

PALM OIL

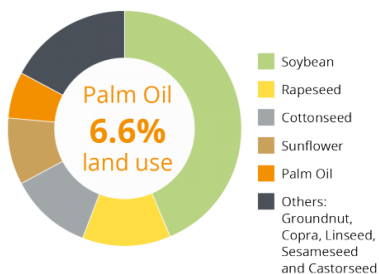


WHAT IS PALM OIL?

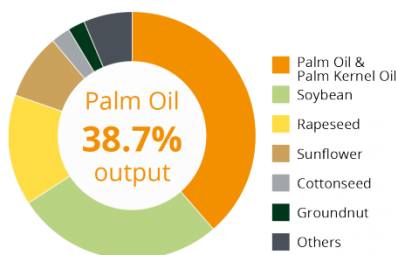
Palm oil is a versatile vegetable oil extracted from the oil palm tree, which can be cultivated at tropical latitudes. A little over 70m tonnes of palm oil were produced globally in 2018; in 1995, global production was just 15m tonnes. The vast majority of this expansion has occurred in Southeast Asia, which is the global centre for palm oil production. In 2018, it was estimated that as much as 25m hectares of land is under palm oil cultivation, accounting for both industrial and smallholder plantations.¹

Despite being native to Africa, oil palm trees were brought to Southeast Asia in the early twentieth century as an ornamental crop; Indonesia and Malaysia are now collectively responsible for around 85-90% of global production.

Major Oilseeds: Area in 2015
(Total is 274.4 million hectares) (Oil World 2016)



Global production of oils and fats in 2015
(Total is 179.6 million tons) (Oil World 2016)

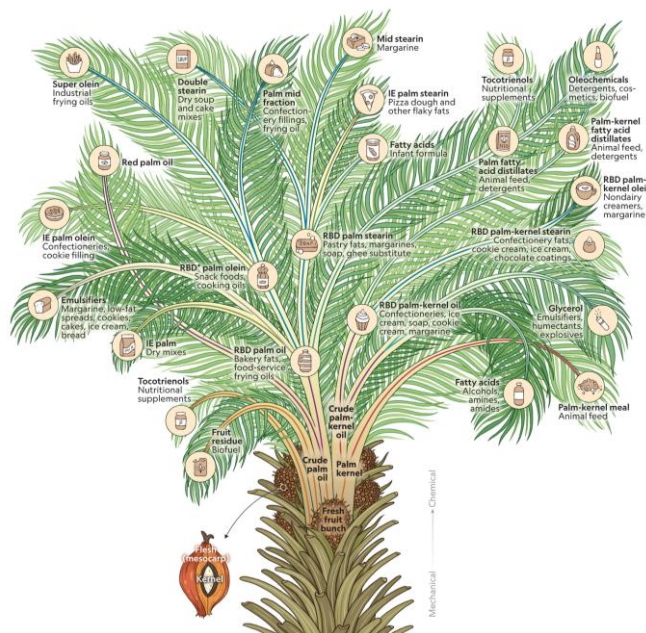


The crop is so popular because it is highly efficient in terms of tonnes of oil produced per hectare under cultivation, achieving yields of 3.8 tonnes per hectare. By comparison, rapeseed oil

has typical yields of 0.8 tonnes/hectare and sunflower oil has typical yields of 0.7 tonnes/hectare. As a result, although oil palm accounts for the smallest percentage (6.6%) of all the cultivated land for oils and fats globally, it produces the largest percentage (38.7%) of total output.² In addition to oil, the oil palm tree yields palm kernel and expeller (cake) which can be used in applications such as biofuels and animal feed.

WHAT IS PALM OIL USED FOR?

Palm oil is among the most versatile of vegetable oils; semi-solid at room temperature, the oil is to be found in approximately 50% of food and non-food products sold in high-street supermarkets. Palm oil's suitability as a frying fat means that it also accounts for around 35% of the world's vegetable oil market, and is a more affordable staple in poorer economies. This is in part because the environmental and social costs associated with its production are not reflected in market prices; instead, they are considered "externalities".



'Tree of Plenty' – the myriad uses for oil palm products. Source: National Geographic / Malaysian Palm Oil Board

¹ <https://www.iucn.org/news/secretariat/201806/saving-no-palm-oil-would-likely-displace-not-halt-biodiversity-loss---iucn-report>

² According to the European Palm Oil Alliance

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It can be found in personal care products and cosmetics (shampoo, soap, makeup etc.), in confectionery snacks, ice cream, margarine and spreads, animal feed, pharmaceuticals, and industrial applications such as greases, lubricants and candles. Its use as a biofuel feedstock has been criticised for some time, due to the substantial environmental footprint of palm-oil-derived biofuel.

As a cooking oil, palm oil is among the richest known sources of Vitamin E (natural tocotrienols) which helps lower 'bad cholesterol' levels. It is also high in natural Vitamin A (carotenoids) that stimulates the immune system, and is free from cholesterol and trans-fats.

WHAT ARE THE RISKS FOR RESPONSIBLE AND SUSTAINABLE INVESTORS?

The environmental and social impacts of palm oil cultivation are wide-ranging. The principal issues have stemmed from poor regulation and enforcement in the main production markets of Indonesia and Malaysia. This has allowed major palm oil companies to expand the area of land under cultivation dramatically since the 1970s. Deforestation³, peatland clearance and burning, land-grabbing, violation of indigenous people's rights and biodiversity loss have gone hand-in-hand with this expansion.

Countless species have suffered, with the precarious existence of the orang-utan being familiar to many. Burning of forests also leads to extreme levels of air pollution, causing widespread health emergencies.

However, an International Union for Conservation of Nature (IUCN) report of 2018 indicated that alternatives to palm oil may be just as (if not more) destructive, chiefly because their

³ The United Nations Environment Programme (UNEP) indicated in 2007 that oil palm plantations are the leading cause of rainforest destruction in Malaysia and Indonesia; and a study by Princeton University and a Swiss institution reported that between 1990 and 2005, up to 60% of palm oil expansion occurred at the expense of primary tropical rain forest. Palm oil production is said to have been responsible for about 8% of the world's deforestation between 1990 and 2008. More recent studies have confirmed these trends and highlighted the continued deforestation which is carried out in order to expand oil palm plantations.

lower yields/hectare will require greater land-use change, potentially in other highly sensitive regions, such as the Amazon.



An image of the devastation caused by palm oil plantation expansion in Southeast Asia, which has had catastrophic impacts on local megafauna and ecosystems more broadly. The Bornean orang-utan is now listed as endangered on the International Union for Conservation of Nature (IUCN) Red List; the Sumatran orang-utan is critically endangered, as is a recently-discovered species, the Tapanuli orang-utan, which is the most endangered of all great apes. The WWF estimates that 60% of wild orang-utans have been killed in the last century – an ecological blink of the eye. Image source: Rainforest Rescue.

The report concluded that "there appears to be no straightforward way to phase out palm oil without incurring potentially more significant environmental and social impacts elsewhere from compensatory expansion of alternative oil crops".⁴ This argument was used by the Council of Palm Oil Producing Countries in early 2019 as it opposed the Malaysian government's proposal to cap palm oil estates at 6m hectares.⁵

TOWARDS "SUSTAINABLE" PALM OIL

The reputational risks from rainforest clearance and the consequent ecological impact – alongside human rights abuses such as land-grabbing, child and forced/bonded labour – resulted in attempts by businesses, NGOs and governments

⁴ Meijaard, E., Garcia-Ulloa, J., Sheil, D., Wich, S.A., Carlson, K.M., Juffe-Bignoli, D., and Brooks, T.M. (eds.) (2018). Oil palm and biodiversity. A situation analysis by the IUCN Oil Palm Task Force. IUCN Oil Palm Task Force. Gland, Switzerland: IUCN, xiii + 116pp.

⁵ <https://www.bloomberg.com/news/articles/2019-03-01/malaysia-plans-to-halt-palm-oil-expansion-to-dispel-bad-image>

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to work towards making palm oil sustainable by certifying the supply chain.

At the heart of change since 2004 has been the Roundtable on Sustainable Palm Oil (RSPO), an NGO and certifying body. Since its inception, the RSPO has gradually increased the area covered by its certification scheme. As at 30 June 2018, that area was 3.2m hectares, representing an annual certified production volume of 13.6m tonnes of certified sustainable palm oil (CSPO). This had risen to 3.75m hectares by 28 February 2019. The RSPO's 2018 Impact Report also highlighted that an area of more than 263,000 hectares of High Conservation Value (HCV) land has been set aside and managed by RSPO members – a 39% increase from the previous reporting year.⁶ Now, an estimated 19% of all palm oil produced globally is certified under the RSPO standard.



Despite this progress, the RSPO has been criticised for failing to improve the industry's sustainable credentials adequately. Indeed, a 2018 study conducted by researchers from the University of Queensland and the ARC Centre of Excellence for Environmental Decisions (CEED), in collaboration with Borneo Futures, suggested that RSPO-certified plantations perform no better than non-RSPO estates on a series of sustainability metrics, including species and habitat conservation, as well as social benefits to local communities.⁷

⁶ Statistics in this paragraph are taken from the RSPO's website and its 2018 Impact Report (see <https://rspo.org/impacts>)

⁷ H.N. Jong, "RSPO fails to deliver on environmental and social sustainability, study finds", *Mongabay*, 11 July 2018.

The RSPO itself, whilst challenging the study's findings, has acknowledged that gaps remain in its understanding of how certification translates to real-world impacts.

The unpalatable truth is that because oil palm trees can only be cultivated in tropical regions, there is a danger that expansion of the industry will be contingent on deforestation.

Yet this is not inevitable. In 2018, *National Geographic* investigated the fledgling palm oil industry of Gabon, in West Africa, documenting the efforts being made by major palm oil companies, the Gabonese government, NGOs, and other stakeholders to develop the industry responsibly, with environmental and social considerations in focus. This includes setting aside large HCV areas of forest, and only developing plantations where impacts are most limited, as part of a national land-use plan. Such a plan seeks to balance the economic needs of the country –which is in fact relatively wealthy by sub-Saharan African standards – with those of local communities and ecosystems. In other words, Gabon is seeking a planned, sustainable palm oil industry, rather than one bent on growth at any cost.⁸

WHAT DO WE LOOK FOR IN COMPANIES WITH EXPOSURE TO THE PALM OIL SECTOR?

Our Amity Funds have no direct exposure to palm oil plantations. Instead, our exposure to the commodity is indirect, chiefly through banks and food producers and retailers. Where these companies have palm oil in their supply chains, or are financing palm oil companies in Southeast Asia and elsewhere, our minimum expectations are for "No Deforestation, No Peat, No Exploitation" policies, and evidence that these are strictly adhered to. Commitments to source certified-sustainable palm oil (as certified by the RSPO) are also essential.



⁸ <https://www.nationalgeographic.com/magazine/2018/12/palm-oil-products-borneo-africa-environment-impact/>

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Help in this regard comes from tools such as SPOTT, (the Sustainability Palm Oil Transparency Toolkit) pioneered by a team at the Zoological Society of London (ZSL), which provides interactive company scorecards across seven indicators including environmental management, zero burning, GHG emissions and traceability. We also consider any human rights violations and evidence of poor environmental policies and practices when (i) screening and reviewing companies with exposure to palm oil; and (ii) engaging with companies with exposure to the sector.

CONCLUSION

Palm oil continues to present responsible and sustainable investors such as EdenTree with a range of environmental and social risks. But, as the IUCN's 2018 report noted, it seems apparent that palm oil is "here to stay". Because of the risks we have articulated, investing in companies with exposure to palm oil – however indirectly – must be done with great care and attention.

The focus of NGOs, consumers, responsible palm oil companies, regional governments, and responsible investors must now be to ensure that deforestation is halted, along with peatland burning, land-grabbing, the persecution of indigenous peoples and flora and fauna, and other human rights abuses associated with the industry. Only then can efforts at the regeneration and rehabilitation of ecosystems and communities be launched from a stable base.

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THE EDENTREE RI TEAM



Neville White
Head of SRI Policy
and Research



Esmé van Herwijnen
Responsible Investment
Analyst



Jon Mowll
Responsible
Investment Analyst

We have a specialist in-house Responsible Investment (RI) team who carry out thematic and stock-specific research to identify ethically responsible investment ideas for our range of Amity funds. Headed up by Neville White, Head of RI Policy & Research, and supported by Responsible Investment Analysts Esmé van Herwijnen and Jon Mowll, the team is also responsible for creating an on-going dialogue with companies, allowing us to engage on a wide variety of ethical and socially responsible investment concerns. Our ethical and responsible investment process is overseen by an independent Amity Panel that meets three times a year, and comprises industry and business experts, appointed for their specialist knowledge.

We hope you enjoy this RI Expert Briefing and find it useful and informative. For any further information please contact us on 0800 011 3821 or at ifa@edentreeim.com