



# Stewart Investors Sustainable Funds Group

## Sustainable Palm Oil?

Second Quarter 2017

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### **Recent forest fires across Malaysia and Indonesia cast a haze over many parts of Southeast Asia.**

Driving these fires was the production of palm oil, one of the most widely used vegetable oils in the world.

Palm oil has a high resistance to oxidation and consequently a long shelf life, making it an ideal ingredient for a variety of products, from detergents to baked goods.

It can now be found in half of all products in a supermarket. It also produces higher yields per hectare compared to other oils, such as rapeseed, sunflower and soy.

### **Palm oil has become a major source of income for local communities and an important part of the rural economy in many countries.**

However, rising demand has led to large-scale conversion of natural forest areas for plantations, resulting in carbon dioxide emissions, loss of high conservation value forests, soil erosion, air pollution, loss of biodiversity, as well as social conflict.

In an effort to address some of these challenges and promote the use of sustainable palm oil through credible global standards, the Roundtable for Sustainable Palm Oil (RSPO) was established in 2004.

There are four types of RSPO certified palm oil, and unfortunately the most common types, GreenPalm and Mass Balance, are not completely deforestation free.

The complete separation of certified and non-certified palm oil is expensive and difficult to achieve. Mass Balance is a cost-effective mixture of certified sustainable palm oil and non-certified palm oil.

GreenPalm allows manufacturers and retailers to buy GreenPalm certificates from an RSPO certified palm oil grower to offset each tonne of palm oil they purchase.

The two other types of RSPO palm oil are Segregated and Identity Preserved, which ensure higher levels of traceability and physical separation of certified and non-certified palm oil.

These are more expensive and not currently available in the quantities required by many large consumer companies. Speedy certification may not always be the answer to solve the issue.

Many companies now require RSPO certification as a minimum but are increasingly finding ways to build on RSPO criteria by working with suppliers to ensure additional protection against forest loss and degradation and social conflict.

### **An encouraging number of companies have made commitments to source sustainable palm oil.**

Putting these goals into action can be arduous, as the palm oil supply chain is vast, complex and relies heavily on small processors and farmers whose palm oil is difficult to trace.

Unilever, one of the world's largest buyers of palm oil, is working to source all of its palm oil from traceable and certified sources by 2020.

To achieve this target, they've started using a tool called Known Sources which allows them to gather information about suppliers and ensure compliance with their Supplier Code.

As of 2014, they achieved 70% traceability to known mills and have visibility of over 1,800 crude palm oil mills.

Henkel is another consumer company which has decided to phase out GreenPalm certificates and is working directly with suppliers to ensure they are at minimum Mass Balance certified.

We hold positions in both Unilever and Henkel in our portfolios.

Our approach to engagement is one that is always based on encouraging companies to protect long-term shareholder value.

Forest fires in Indonesia continue to heighten the focus on deforestation and the multinational consumer goods companies purchasing palm oil are an easy target for concerned stakeholders.

### **However, large volumes of palm oil are also purchased by emerging markets consumer companies.**

Engagement with these companies can be more challenging because consumers are less engaged and NGOs (non-governmental organisation) less influential. However, we see this gradually starting to change.

While not targeting palm oil, Singapore supermarket operators, including Sheng Siong which we hold in some of our Asia portfolios, stopped sourcing paper products from listed company Asia Pulp & Paper due to concerns around their green credentials in light of the Indonesian forest fires.

We believe this may be a sign of things to come from a more environmentally engaged Asian community.

### **We are convinced that companies that choose to strengthen their supply chains will minimise risk and be better placed over the long run to deliver improved shareholder value.**

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