UNIVERSITY OF CAMBRIDGE
INSTITUTE FOR
SUSTAINABILITY LEADERSHIP

Business Briefing

Banking Beyond Deforestation

How the banking industry can help halt and reverse deforestation

Summary of full report

Nature is in decline

More than 50 per cent of global GDP relies upon services provided by nature, including freshwater, healthy soil and clean air.[1]

Despite this, nature is experiencing a precipitous decline. One million species are threatened with extinction[2] and every six seconds, a football pitch of 'primary forest'[i] is lost.[3] The Covid-19 pandemic has underscored the urgency of tackling the deforestation challenge, with habitat loss increasing the likelihood that viruses transmit from animals to humans.[4]

Halting and reversing deforestation remains an issue that needs focused action by organisations along the value chain, including banks. This paper focuses on soft commodity-related deforestation.

How banks are connected to soft commodity-related deforestation

Soft commodities such as palm oil, soy, beef and timber products are responsible for the majority of deforestation caused by commercial agriculture.[5] Banks provide a variety of finance and financial services to enterprises along soft commodity supply chains, from term loans, trade finance and revolving credit facilities, to bond and fund structuring, capital raising, project finance and more.

The 'Soft Commodities' Compact

The 'Soft Commodities' Compact ('Compact') was a company-led alliance between CISL's Banking Environment Initiative (BEI) and the Consumer Goods Forum (CGF), the goal of which was to lead the banking industry in aligning with the CGF's resolution to help achieve zero net deforestation by 2020.

Despite this resolution and other global efforts, deforestation has not been halted. Yet because of the public commitment, Compact banks grew their understanding of deforestation risk and have created leading positions for the industry. Using Technical Guidance developed in consultation with banks and other stakeholders, banks established anti-deforestation policies and began reporting compliance levels. Today, Forest 500 ranks Compact adopters amongst the most advanced in terms of 'policy' – all are in the top 30 of 150 financial institutions.[6]

In addition to raising banking standards, the Compact committed to financing the transformation of supply chains.[7] Individual examples of leadership have emerged, with Compact adopters, BNP Paribas, pioneering the Tropical Landscape Financing Facility, and Rabobank a driving force behind the Agri3 Fund. Both provide concessional finance that improves rural livelihoods and promotes sustainable agriculture.

Thanks to C-suite support of the commitment, all 12 adopter banks have remained engaged throughout the six year collaboration, despite changes in personnel and different skillsets being needed at different stages. The commitment also made a wider programme of work possible on sustainable supply chains and finance, where CISL convened stakeholders, conducted research and

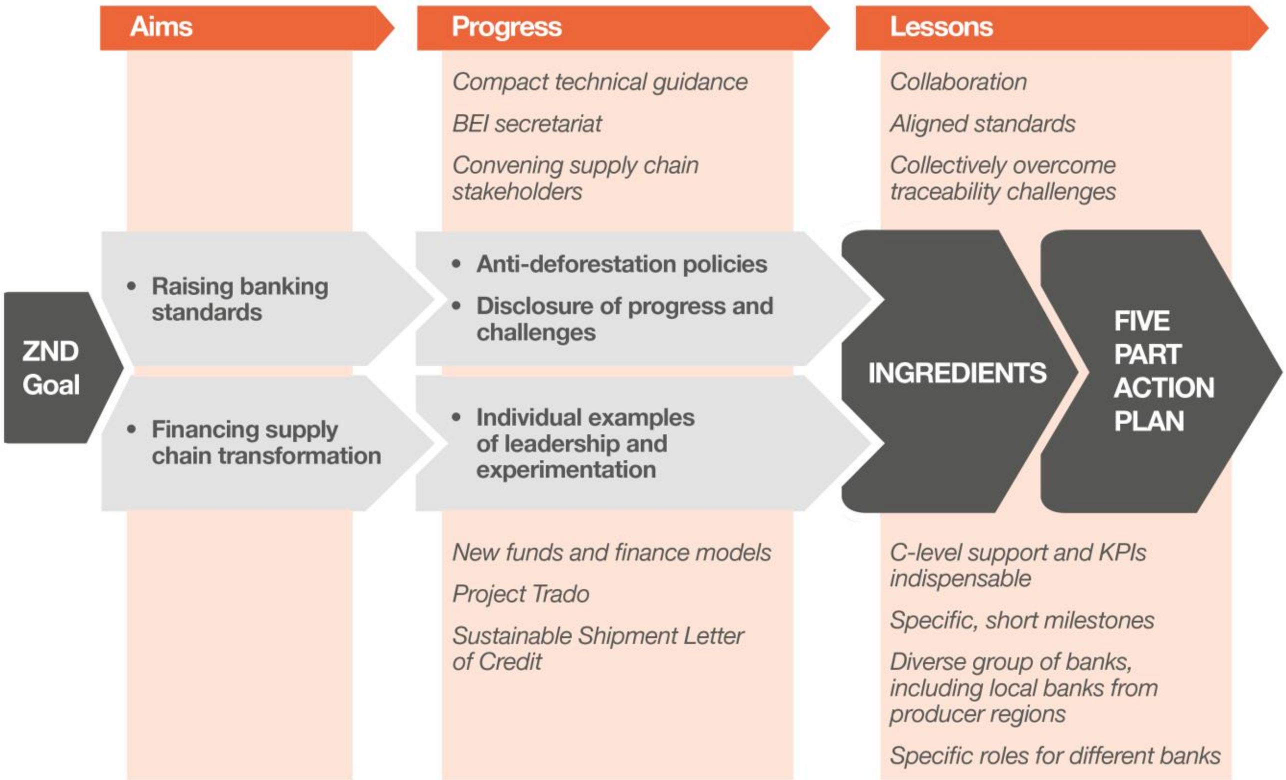
[i] Primary forests are 'forests in their final form', meaning a fully mature forest that can take hundreds to even thousands of years to establish itself.

delivered pilot transactions testing how financial mechanisms could transform supply chains. The programme of work included:

- Sustainable Shipment Letter of Credit (2014)
- Sustainable Trade Finance Council (2015)
- Greening the finance of China's commodity imports (2016)
- Catalysing Fintech for Sustainability: Lessons from multi-sector innovation (2017)
- Trado: New technologies to fund fairer, more transparent supply chains (2019)

The progress made and lessons learnt during the Compact have been used to create a five-part Action Plan for a diverse group of local, regional and global banks to combat deforestation.

Aims, progress and lessons from the 'Soft Commodities' Compact



How banks can help halt and reverse deforestation

Banks can be intermediaries for financial incentives that grow the supply of 'deforestation-free'[ii] or 'forest restorative'[iii] soft commodities. This is because banks have:

- access to businesses along the supply chain and to diverse sources of capital, such as investors seeking impact;

[ii] Commodity production, sourcing, or financial investments that do not cause or contribute to deforestation (as defined by the Accountability Framework Initiative)
[iii] Land management that leads to the restoration of forest. It could involve restoring degraded farmland with agroforestry at the producer level or larger areas of natural habitat at the landscape level.

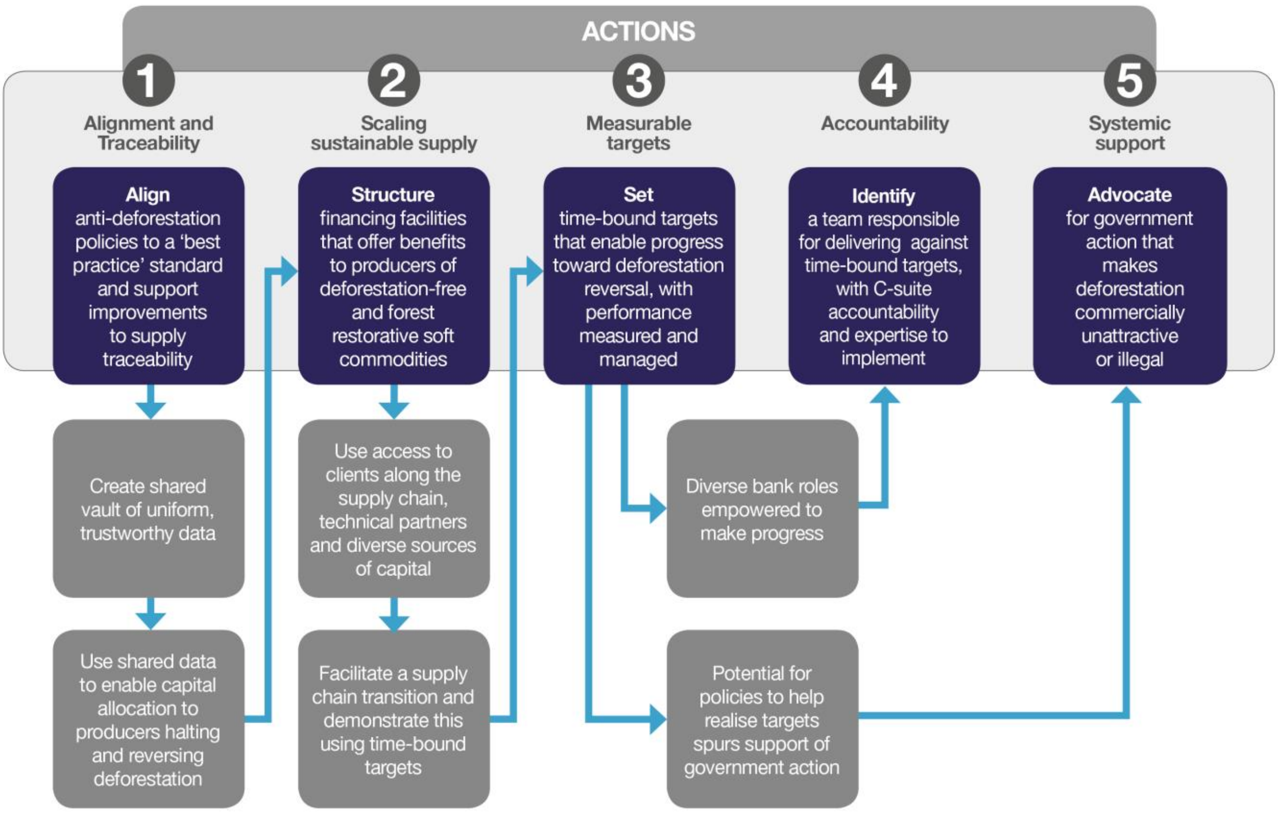
- expertise to assess counterparty risk and structure capital;
- data about client operations

These three levers mean banks can:

1. Support improvements to soft commodity traceability by working with clients to implement anti-deforestation standards.
   - Banks can use their access to businesses along the supply chain and data gathered in risk management processes to assemble information about the nature of soft commodities produced or handled by clients.
2. Mobilise and structure funds that channel finance and incentives to soft commodity producers in exchange for commodities that are deforestation-free or forest restorative.
   - Banks can act as intermediaries, using their access and structuring expertise to connect producers with capital that incentivises sustainable production.

By contributing in these ways, banks support broader efforts in the economy to decouple soft commodity production from deforestation and gather the data that proves it.

Five part Action Plan for banks to support the halting and reversal of deforestation



The first action is for the banking industry to align anti-deforestation policies to best practice standards. This can facilitate data verification by multiple banks, enabling them to populate a shared data vault with collective knowledge about deforestation risk along the supply chain. This vault can then be used to identify opportunities for banks to support clients to remove deforestation from soft commodities produced or purchased.

This support for clients comes in Action 2, in the form of financial benefits that incentivise production of deforestation-free or forest restorative soft commodities and pay for data that proves the status of supply. Banks play a facilitation role, mobilising and structuring the benefits and underlying finance to which they are attached. They can also source funds to pay for those benefits from impact investors, government, development banks and corporate off-takers.

To make progress, accountability and public time-bound targets are essential. Action 3 details specific time-bound milestones to make halting and reversing deforestation possible and Action 4 pinpoints suggested roles for implementation.

By publicly setting robust targets, it becomes in the interest of banks to advocate for supportive global policy. As explored in Action 5, by occupying the role of facilitator, banks rely on other parties, including governments. A supportive policy landscape can spur action along the supply chain.

A supportive context exists for action

A more supportive external context now exists for ambitious action. From remote sensing to the mandated disclosure of financed emissions to a growing appetite from banks' clients in forest restoration, there is today an enabling context for banks to create financial solutions that support clients' transition to producing or handling deforestation-free soft commodities.

The need for collaborative action amongst banks

The bedrock of this Action Plan is collaboration between local, regional and global banks along the supply chain. By collaborating, these banks share costs and expertise, enhance due diligence, reduce the likelihood that deforestation leaks to another financier and can create standardised, scalable financial solutions that reduce transaction costs and enable scale.

Halting and reversing deforestation requires a wide variety of stakeholders

While the external context for action has improved, systemic change cannot be achieved by banks acting alone. This Action Plan casts banks as facilitators, working with peers, clients and stakeholders to channel increasing flows of capital towards deforestation-free and forest restorative soft commodity production – and gathering the data to prove it. As the facilitator, however, banks rely on other parties for support:

Action 1 – Alignment and Traceability

- Clients along the supply chain, to grant access to data about the origin and nature of supply produced or handled.
- Traders, to work towards anti-deforestation standards for their trades and financing.
- Companies (bank clients), to implement and verify anti-deforestation actions in their operations and supply chains.
- Technical partners, to ensure that 'best practice' anti-deforestation standards are acceptable and attainable.

Action 2 – Scaling Sustainable Supply

- Local NGOs, cooperatives and government, to help build a viable, scalable pipeline of producers interested in transitioning if supported with financial benefits.
- Providers of capital, to fund financial benefits that support and incentivise producers to transition.
- Technical partners to design and implement transition plans for producers.

Action 3 – Measurable Targets and Action 4 – Accountability

- Technical partners to train the Implementation Team within the bank so they are empowered to deliver time-bound targets.

Action 5 – Systemic Support

- Industry alliances, to provide a platform to promote the aims of the collaboration and organise calls to action.
- Governments and regulators, to set higher expectations about soft commodities that increase the flow of capital toward deforestation-free and forest restorative commodities.

What banks can achieve by taking action

By taking the five actions detailed above, banks can:

- Become part of creating the solution to deforestation, rather than waiting for others to define standards.
- Construct a pipeline for capital capable of scaling sustainable soft commodity production.
- Provide corporates, philanthropic foundations, governments and other stakeholders with additional opportunities to support producers transition, improve livelihoods and reverse deforestation.
- Help prove the origin and sustainability characteristics of soft commodity supply and the impact of deforestation-free financing to a higher degree of confidence.
- Encourage higher standards and expectations across soft commodity sectors in halting and reversing deforestation.

Next steps

Focused global collaboration from all parts of the value chain will be needed to succeed in halting and reversing deforestation.

The diverse group of banks and other stakeholders needed to deliver the Action Plan has yet to be formed. This Plan aims to catalyse banks and stakeholders toward action.

During 2021, CISL will seek expressions of interest from the wider financial sector, corporates, NGOs, policymakers and funders to together develop and implement the Action Plan.

--- The full *Banking Beyond Deforestation* report can be read here ---

The University of Cambridge Institute for Sustainability Leadership

The University of Cambridge Institute for Sustainability Leadership (CISL) is a globally influential Institute developing leadership and solutions for a sustainable economy. We believe the economy can be 'rewired', through focused collaboration between business, government and finance institutions, to deliver positive outcomes for people and environment. CISL convenes the Banking Environment Initiative, created in 2010 by the Chief Executives of some of the world's largest banks. The BEI's mission is to lead the banking industry in collectively directing capital towards environmentally and socially sustainable economic development.

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