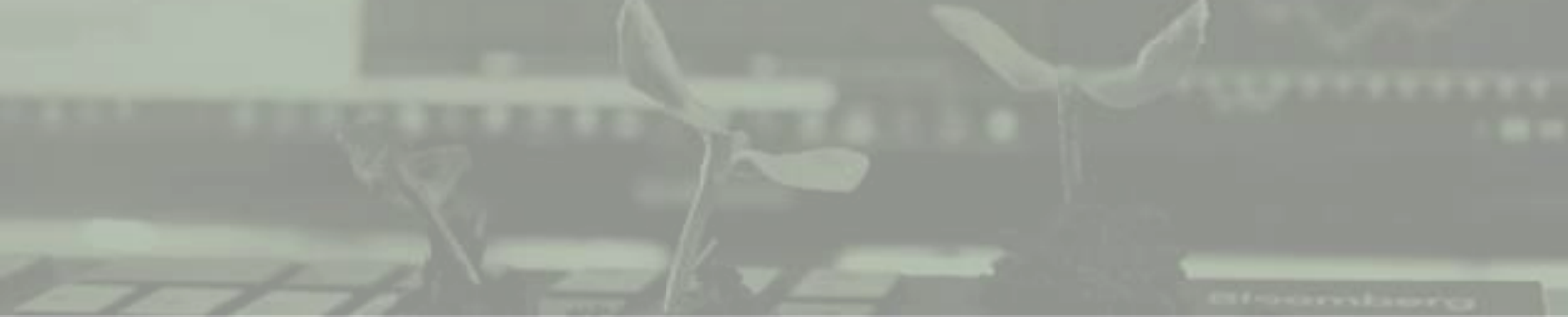


ICA Gruppen green bond: deforestation risk

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Food retailers globally play an important role in driving their supply chains to mitigate biodiversity loss, deforestation and climate change.[1] ICA Gruppen (Ticker: ICASS, not rated) is Sweden's leading food retail chain, with a market share of approximately 36%.[2] The company is now in the market for an inaugural SEK 2-3Bn green bond.[3,4] The vague supply chain targets included in the use-of-proceeds should give pause to investors focused on sustainability impact, given ICASS' relatively mediocre performance in this area to date. As ICA Gruppen is now a private company, debt investors have an outsized role in influencing the ambition of this company.

ICA Gruppen has clear potential to improve on its main environmental footprint, the deforestation and biodiversity impact of its supply chain. The retailer has been given a low score of 1/5 by Forest500, and only 4/90 when it comes to beef sourcing (2021). The company is ranked 132/350 in the Food and Agriculture Benchmark[5] and 32/56 in the Ecogain Biodiversity Index 2020, which grades large Scandinavian corporates.

The use-of-proceeds of the proposed green bond go into four main categories: green building, renewable energy, clean transport and "eco-efficient and/or circular economy adapted products." There seem to be few issues with the first three but there are several questions for investors relating to sustainable food chains, including:

- Why has the issuer not considered more ambitious or precise targets to ensure that the bond ranks higher than the current "light green"?
- How do the targets/KPIs relate to requirements set by the recently enacted EU Deforestation Regulation?[6]
- The low rankings of the issuer from many of the leading providers in the biodiversity space make it hard to invest in the name from a quantitative portfolio allocation angle. Will there be remedies to this, and what will those be?

A successful and highly profitable food retailer in Scandinavia is in a strong position to have a market-leading green bond framework with ambitious use-of-proceeds in terms of biodiversity/food supply chain impact. In its current state, we ask investors to consider if the ICASS proposal gets there.

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[1] "Addressing Biodiversity in Food-based Sectors", Amundi Institute, 29 Mar 2023.
[2] "ICA Sweden– Sweden's leading grocery retailer", ICA Gruppen Website, accessed 8 May 2023.
[3] FIGI - 3y fixed: BBG01GL35CH3/ 3y FRN: BBG01GL35CL8 / 5y fixed: BBG01GL35CN6 / 5y FRN: BBG01GL35CW6.
[4] DANSKE, SHB and SEB are acting as joint bookrunners and holding calls with fixed income investors. In February, ICASS issued SEK 3.5bn of bonds across 2025 and 2027 tenors and mixed in fixed/FRN format.
[5] Ranking by the World Benchmarking Alliance.
[6] E.g. see "Cargill: EUR bond, EU deforestation regulation", AFII, 14 Apr 2023.

Not investment advice. This version 10 May 2023. Important disclaimers at end of the document. One of the authors served on the Board of Cicero Shades of Green, the SPO provider on the bond, until the company was acquired by S&P Global in Nov 2022.
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ICA Gruppen existing debt

ICA Gruppen is an irregular issuer with six unrated outstanding bonds worth SEK 5.00 bn. The company last came to market in February 2023 with a mix of four fixed/FRN bonds across 2- and 4-year tenors (see Table 1). The forthcoming issuance will be its inaugural green bond offering and make up approximately 40% of its outstanding bonds. The company went private in November last year after being acquired by a consortium led by AMF Tjanstepension AB.[7]

Table 1. ICA Gruppen outstanding bonds. Source: Bloomberg - accessed 9 May 2023.

Description	ISIN	Issue Date	Maturity	Currency	Amount Outstanding (SEK)	Amount Outstanding (EUR)
ICASS Float 03/25/24	SE0013882909	25-Mar-21	25-Mar-24	SEK	115,504,000	98,100,000
ICASS Float 02/24/25	SE0013883931	24-Feb-23	24-Feb-25	SEK	104,722,420	99,290,000
ICASS 4.9 02/24/25	SE0013883956	24-Feb-23	24-Feb-25	SEK	38,080,880	36,110,000
ICASS Float 02/28/25	SE0012676740	28-Feb-20	28-Feb-25	SEK	51,627,500	46,930,000
ICASS Float 02/24/27	SE0013883949	24-Feb-23	24-Feb-27	SEK	133,283,080	126,370,000
ICASS 4.905 02/24/27 #DMTN	SE0013883964	24-Feb-23	24-Feb-27	SEK	57,121,320	54,160,000

Complying with EU Deforestation Regulation

Investors are increasingly encouraged to adopt strong biodiversity and nature loss guidelines.[8] By 2025, ICA Gruppen will have to comply with the recently adopted EU Deforestation Regulation.[9]

The regulation on deforestation-free products requires companies selling to Europe products exposed to commodities such as soy, palm oil, cocoa, beef, coffee or timber products to have proof that they do not contribute to deforestation in the EU and elsewhere. Operators including retailers will need to submit due diligence statements to the member states' competent authorities and provide information such as geolocation coordinates of where the products were produced.[10]

The regulation will be reviewed in 2024 to include additional commodities and ecosystems and enforced in 2025.

Companies failing to comply with the regulation may face fines of up to 4% of their annual turnover, and face reputational damage in an environment where consumers are increasingly mindful about environmental footprint.[11] In light of the significant financial risk to investors, they will need to carry out a thorough due diligence of potential investee companies as part of their fiduciary duties.

Retailers' exposure to deforestation risk can be significant. Global environmental organisation Mighty Earth recently released an investigation showing evidence of direct links between UK supermarket chain Tesco and Brazilian deforestation.[12] Similar issues have also been reported for other UK retailers.[13]

[7] "Swedish Grocer ICA to Go Private at $12.5 Billion Valuation", Bloomberg, 10 Nov 2021.
[8] "Kunming-Montreal agreements: A bond perspective", AFII, 5 Apr 2023.
[9] "Parliament adopts new law to fight global deforestation", European Parliament News, 19 Apr 2023.
[10] "A high-level introduction to the EU Deforestation-Free Regulation (EUDR)", KPMG, 15 Feb 2023.
[11] "Assessing the financial impact of the land use transition on the food and agriculture sector", UNFCCC, Sept 2022.
[12] "Tesco: A basket of problems for the Amazon.", Mighty Earth, Apr 2023.
[13] "UK meat industry and supermarkets including Tesco, Asda, Sainsbury's and Morrisons 'causing illegal deforestation in the Amazon'", Sky News, 13 Apr 2023.

ICA Gruppen's strategy to tackle deforestation in its supply chains has been questioned: e.g., "[ICA] has not made any commitments to zero-gross deforestation or conversion for any of its commodities."[14]

The company has a commitment to have its cocoa, coffee, seafood, palm oil, soy and cotton products in its corporate brands certified by 2025 but certification schemes are inconsistent and offer variable deforestation-free assurances.[15],[16] Moreover, the commitment does not extend to third-party brand names.

Despite being part of initiatives such as the "Consumer Goods Forum"[17], the company has not made any explicit commitments to achieving zero-deforestation for any of the aforementioned commodities and offers limited details on the steps it intends to take to establish traceability across its supply chains.

Forest500 - a global initiative assessing and ranking efforts of companies and financial institutions to address deforestation – gives ICA Gruppen one of the poorest scores amongst the European retail sector as illustrated in Table 2.

The company received a 2022 deforestation score of F from CDP (on a scale A-F) for its failure to provide sufficient information on its deforestation strategy and reporting.[18]

Table 2. Forest500 deforestation score assessment of the European food retail sector for the year 2021. Source: Forest500.

Company Name	Forest500 score
Carrefour Group	49%
Casino Guichard Perrachon S.A.	32%
Ahold Delhaize	31%
Association Familiale Mulliez (AFM)	26%
ICA Gruppen AB	15%
SPAR International B.V.	3%

Biodiversity - eligible project questions

The Second Party Opinion (SPO) provider on the bond is lukewarm about the eligible projects related to private label certified products, "eco-efficient and/or circular economy adapted products". [19]

Cicero Shades of Green/S&P assigns a "medium green" rating to the first three categories of green buildings, renewable energy and clean transportation, but gives only a "light green" rating to products. The SPO recognises weaknesses and limitations to the company's ability to measure and mitigate environmental impact in its supply chains.

Eligible projects for the company will include "*expenditures for the group's private label. As a KPI for impact "% of sales from certified products out of total sales of private label products*"".

First, investors should question why the company is limiting its certification efforts solely to its private label. Second, there can be a debate about whether expenses related to standard operations of a company and covering the entire cost of a product should be considered eligible

[14] "Tackling the deforestation on supermarket shelves", Global Canopy, 27 Apr 2022.
[15] As an example, the 2019 "Setting the bar for deforestation-free soy in Europe" report from Profundo highlights discrepancies in soy certification schemes' interpretation of deforestation and implementation.
[16] A full list of certification schemes can be found on the company's " 2022 annual report".
[17] ICA Gruppen's initiatives and membership, accessed on the 9th of May 2023
[18] ICA Gruppen Forest 2022 Assessment, accessed on the 9th of May 2023.
[19] ICA Gruppen AB Green Financing Second Opinion, Cicero Shades of Green, 8 May 2023.

under a green bond program,[20] particularly when the financing is not limited to certified materials. As mentioned in the SPO, "The scope and generality of the specific project category […] increases the lack of transparency and comparability in what these proceeds actually finance."

In conclusion, the market should be aware of weaknesses related to green bonds that purport to align with biodiversity and responsible consumption objectives but may fail to comply with the European Union Regulation on Deforestation due to insufficient commitments and vague strategies.

[20] The logic for the green bond use-of-proceeds for this is from our understanding along these lines: Assume that ICA on average (on an annual basis) has SEK 500mn of goods that is has paid for but not yet made into products in its private label. Then assume that SEK 100mn of those goods are sourced in a way that is aligned with the GB framework. Then the 100mn is an "asset" on balance sheet, that could be matched by a liability/debt in the form of a green bond.

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