Deforestation exposure: Q2 & Q3 2024 issuance review

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In the fixed income space, companies' exposure to deforestation risk is becoming increasingly important to the investment community.Figure 1 Issuance from AFII's Representative Deforestation Credit Portfolio averages $17.6bn per quarter since 2016, demonstrating its significance for investors (see Figure 1).[1]

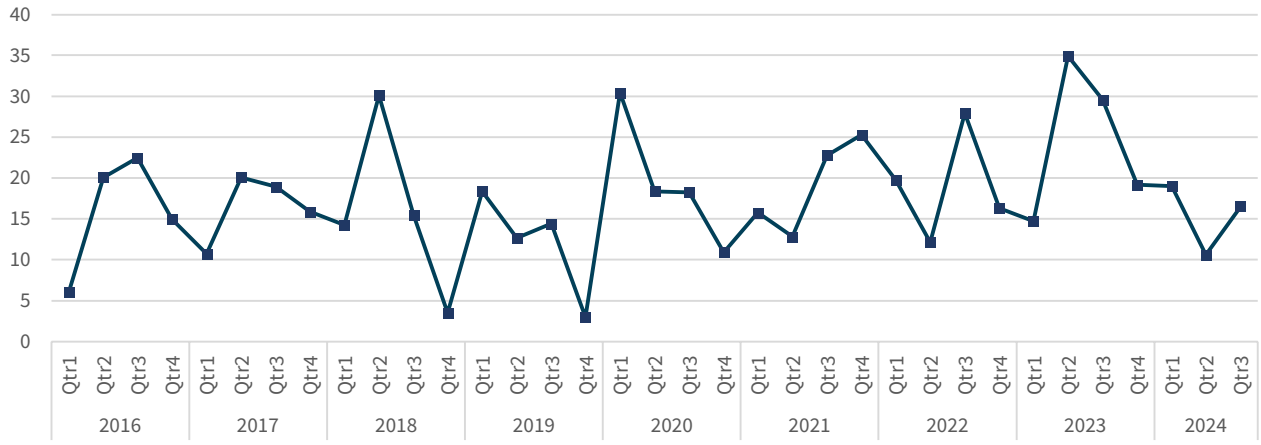
Recently, ShareAction, an NGO, and the UN Environment Programme World Conservation Monitoring Centre (UNEP-WCMC) published guidelines for nature-friendly investment.[2]

In addition, the Taskforce on Nature-related Financial Disclosures (TNFD) — an initiative that provides guidance and recommendations to businesses and financial institutions on how to assess, report, and address nature-related risks, impacts, and opportunities — saw a 30% increase in the number of adopters since January of this year.[3]

This report considers recent fixed income issuance from companies potentially exposed to deforestation to help investors in understanding how their exposure may have changed.

- USD issuance has been high, driven by a large deal from Kroger. **Benchmarked investors have potentially increased their exposure to deforestation as a result.**
- EUR issuance is roughly in line with the broader market, however there are significant issuances from non-EU companies, **which is a chance for non-domestic engagement**.
- **ESG-labelled bond issuance has reduced**. More use of these structures would increase transparency and investor dialogue in environmentally important sectors.

Figure 1. Total issuance from AFII's Representative Deforestation Credit Portfolio in $bn. Source: Bloomberg, accessed 2 Oct 2024.



[1] The original paper can be found at "RDCP: Deforestation exposure in liquid credit portfolios", AFII, 22 Dec 2023.

[2] "Risk Management in Protected Areas", ShareAction, 10 Sep 2024.

[3] "TNFD adoption now over 400 organisations and new sector guidance released", TNFD, 28 Jun 2024.

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Representative Deforestation Credit Portfolio

To improve transparency into potential fixed income exposure to deforestation, AFII developed the Representative Deforestation Credit Portfolio (RDCP) universe. The RDCP universe comprises 35 companies, all issuers of fixed income securities, that are potentially relevant for credit portfolio managers seeking to understand their deforestation exposures.[1]

Potential deforestation exposure is estimated by considering the relevance of agricultural supply chains, the public commitments made by an issuer, and the financial materiality of exposure. A fixed income specific liquidity check is overlaid, to ensure the universe is relevant for bond investors.

A full list of the current universe is shown in the Appendix in Table 1, alongside their respective AFII Deforestation Scores (ADS). For full details on this scoring, please refer to the original white paper.[1]

Q2 2024 and Q3 2024 issuances

At the end of Q1 2024, we reviewed issuance from the RDCP universe to understand how a benchmarked investor's potential exposure to deforestation may have changed over time. In the first quarter of this year, volumes of USD BBB issuance lagged the market while EUR BBB issuance was ahead. The most significant issuances came from Ahold, a Dutch-Belgian supermarket,[4] and Kraft-Heinz, a US food company.

Looking at the last six months, 18 RDCP issuers came to market, with a total of $24bn of new debt.

There were transactions in seven currencies (EUR, USD, BRL, CHF, JPY, GPB, CAD). Full details are in the Appendix in Table 2.

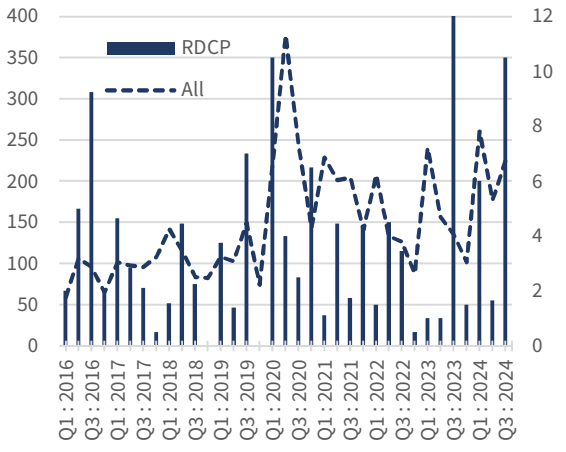
We will now compare BBB issuance across EUR and USD to the overall market to discern trends.

USD issuance

Figure 2 compares the total USD-denominated issuance of the BBB-rated RDCP universe with all USD BBB bonds.[5] Since the last update of the RDCP in Q1 2024, overall bond market issuance has remained high relative to the past three financial years, possibly because of reducing rates.

However, the RDCP universe saw below average issuance in Q2 2024 and above average issuance in Q3 2024, a quarter which also witnessed the second highest issuance in our sample since Q1 2016.

Figure 2. USD BBB issuance in $bn by pricing date. Source: Bloomberg, accessed 1 Oct 2024.



The biggest RDCP deal in the last two quarters was from Kroger, a major U.S. supermarket chain offering groceries, pharmacy services, and general merchandise. It issued a seven-tranche deal of two, three, five, seven, 10, 20, and 30 year

[4] For analysis on this bond deal please see "Relative value is in the eye of the Ahold-er", AFII, 18 Mar 2024.
[5] BBB rating is chosen as the most typical rating of corporate issuers.

bonds worth $10.5bn in Aug 2024 to fund an acquisition.[6] Kroger's potential forest risk comes from its use of the commodities palm oil, soy, beef, timber, and pulp & paper, all of which may contribute to deforestation.[7]

We track syndication fees generated from deals with RDCP issuers to support bank engagement.[8] The joint lead managers for this significant transaction were Citi, Wells Fargo, Mizuho, Truist Securities, and US Bancorp, the first two of which generated the highest proportion of their fees from issuers potentially exposed to deforestation.[9]

Among non-BBB rated issuers, Unilever, a global consumer goods company, was the biggest issuer (second only to Kroger) in the last two quarters. It priced a three-tranche deal of total size $1.92bn rated A+. Unilever's exposure to deforestation comes through its use of of five deforestation risk commodities: palm oil, soy, beef, and cocoa. It also uses pulp & paper for packaging.[7]

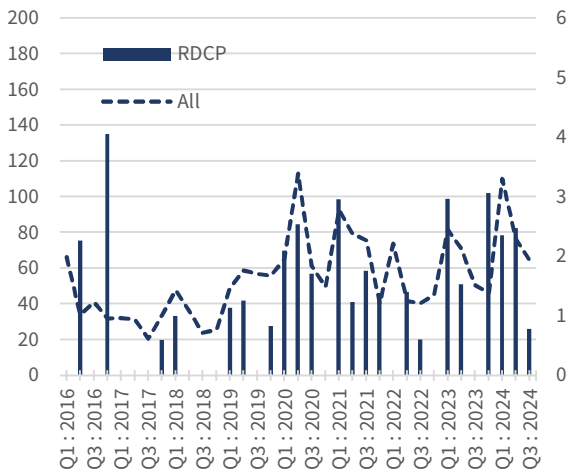
Overall, 72.5% of USD issuance was from companies whose primary jurisdiction was the US.[10] Non-US issuers in USD were Restaurant Brands (the owner of Burger King), Cencosud (a Chilean retailer), Marubeni (a Japanese trading company), and Unilever (a UK-based consumer-based manufacturer).

USD benchmarked investors have potentially increased their exposure to deforestation through Q2 2024 and Q3 2024, mainly due to the $10.5bn Kroger issuance in Aug 2024.

EUR issuance

Figure 3 shows the total EUR-denominated issuance from the BBB-rated RDCP universe compared to all EUR BBB bonds. In contrast to the USD market, total bond issuance has fallen every quarter since Q1 2024 in the EUR market. However the RDCP has not quite followed suit, increasing slightly between Q1 2024 and Q2 2024 before falling to comparable levels to the overall market in Q3 2024. Overall RDCP issuance appears roughly in line with the market.

Figure 3. EUR BBB issuance in $bn by pricing date. Source: Bloomberg, accessed 1 Oct 2024.



The biggest deal across all ratings within the RDCP was from Danone, a multinational food and beverage company. It issued two bonds worth €0.7bn each. Danone is potentially exposed to forest risk through use of palm oil, soy, and the use of pulp & paper for packaging.[7]

General Mills, Inc., a multinational food company that produces and markets a wide range of consumer foods, issued bonds in Q2 2024 worth €0.5bn each maturing in six-and-a-half and 10

[6] "Kroger Sells $10.5 Billion of Bonds to Fund Albertson Buy", Bloomberg, 20 Aug 2024.
[7] "Forest IQ Access the open data", Forest IQ, accessed 3 Oct 2024.
[8] For the white paper please see "The Box: a tool for bank influence", AFII, 20 Dec 2023.
[9] "The Box: syndication fee league table Q3 24", AFII, 17 Sep 2024.
[10] As defined by Bloomberg's 'Country of Risk'. Note this includes $0.35bn issuance from Nestle which Bloomberg reports with the US as its country of risk.

years, respectively. General Mills is potentially exposed to deforestation through use of palm oil, cocoa, soy, and using pulp & paper in its packaging.[7]

Under 50% of EUR RDCP issuance came from companies whose primary jurisdiction was in the EU (as defined by Bloomberg). Non-EU EUR issuance came from Compass Group (a UK-based catering company), General Mills (a US-based global food company), Glencore (a metals and mining company designated as an Australian risk by Bloomberg but headquartered in Switzerland) and Reckitt Benckiser (a British-Dutch consumer goods company designated as UK by Bloomberg).

For EUR investors, RDCP issuance seems roughly in line with the overall BBB market, although there are some significant deals from non-EU issuers that may be of interest to deforestation-minded investors.

ESG-labelled issuance

ESG-labelled bonds comprise securities whose proceeds are reserved for specific projects (called Use-of-Proceeds bonds, or green, social, or sustainable bonds depending on the funded projects), and Sustainability-Linked Bonds (SLBs), where failure to meet a sustainability target usually results in a coupon step-up.

There have been two labelled bonds issued in the last six months by RDCP companies, which together account for 5.0% of the total issuance. We note that both ESG-labelled issuances were in September, meaning that by quarter, they represent 0% of Q2 issuance and 8.3% of Q3 issuance.

Compass Group plc, a British multinational contract food service company, issued a sustainable bond on 16 Sep 2024 worth €0.5bn. This is the third time it has issued sustainable bonds, having also issued in Sep 2022 and Jan 2024. Its financing framework allows six categories of investment.[11] Three are green and three are social. Its latest allocation report shows that as of Oct 2023 investment was focused on sustainable procurement and increasing plant-based products.[12]

Also of note, the French multinational retail corporation Carrefour issued a SLB on 17 Sep 2024. The bond has two Sustainability Performance Targets (SPTs) - to decrease greenhouse gas (GHG) emissions by 50% relative to a 2019 baseline, and to decrease food waste by 55% versus 2016. Failure to meet either SPT will result in a coupon step-up of 25 basis points from 3.625%.[13] This marks Carrefours' sixth SLB, indeed all debt issued by Carrefour SA since Mar 2022 has been in this format.[14]

Elo, the owner of French retailer Auchan, issued a vanilla security in this period despite having issued an SLB in Sept 2023.[15]

In Q1 2024 total ESG-labelled debt was 11.2% of total RDCP issuance, so this period does reflect a reduction. However, it is in line with the market as a whole where total ESG-labelled issuance was

[11] "Sustainable Financing Framework", Compass, accessed 3 Oct 2024.
[12] "Sustainable Bond Allocation Report", Compass, Oct 2023.
[13] "Success of a 750 million euros 8-year Sustainability-Linked Bond", Carrefour, 10 Sep 2024.
[14] For full analysis of the structure please see "A review of Carrefour's Sustainability-Linked Bonds", AFII, 18 Sept 2024.
[15] "Le SLB d'Auchan, il change la vie?", AFII, 22 Sep 2023.

5.0% in H1 2024.[16] Given the climate impact of deforestation, it would be positive to see high adoption of ESG-labelled debt amongst these issuers.

ESG-labelled issuance in this universe has reduced, and this represents an opportunity for investors to engage with companies, especially those that have used labelled structures in the past.

Conclusions

Investor interest in nature-friendly and deforestation risk-free investments continues to grow.

Our review of recent issuance from companies with potential deforestation-exposure offers the following conclusions:

- USD issuance has been high. Volumes were driven by significant acquisition financing from Kroger, a US supermarket chain. The fees from this transaction also dominated Q3 2024 syndication fee league tables.[9]
- EUR issuance appears in line with the overall market, however over 50% of EUR-denominated issuance from the RDCP universe was from issuers whose primary risk jurisdiction is outside the EU. EU-based investors may have increased exposure to these entities.
- Use of ESG-labelled structures was lower, although still in line with the market. These structures are an opportunity for issuers to improve transparency around their sustainability objectives, and for investors to engage directly on those strategies.

There is an opportunity for investors to support more labelled debt issuance in an environmentally important area.

[16] This includes aligned, pending and non-aligned issuance as reported in "Sustainable Debt Market Summary H1 2024", Climate Bonds Initiative, Aug 2024.

Appendix

Table 1. RDCP universe as December 2023.[1] Source: AFII.

Issuer	Ticker	Sub-sector	Country of Risk	Agg. Rating	ADS*
Ahold Delhaize	ADNA	Food & Drug Stores	NL	BBB	10
Aramark	ARMK	Food Services	US	B+	7
Archer-Daniels	ADM	Agri. Prod. Whslrs	US	A	12
Brands Int/Burger King	BCULC	Food Services	CA	BB	8
Cargill	CARGIL	Agri. Producers	US	A	11
Carrefour	CAFP	Food & Drug Stores	FR	BBB+	9
Cencosud	CENSUD	Food & Drug Stores	CL	BBB-	8
Colgate-Palmolive	CL	Personal Care	US	AA-	6
Compass	CPGLN	Food Services	GB	A-	9
Danone	BNFP	Packaged Food	FR	BBB+	7
ELO / Auchan	ELOFR	Food & Bev. Whslrs	FR	BBB-	9
Frigorifico Concepcion	FRICON	Agri. Producers	PY	B	10
General Mills	GIS	Packaged Food	US	BBB	9
Glencore	GLENLN	Base Metals	AU	BBB+	10
JBS	JBSSBZ	Packaged Food	US	BBB-	8
Kering	KERFP	Apparel, Footwear	FR	A	8
Klabin	KLAB	Paper	BR	BB+	14
Kraft Heinz	KHC	Packaged Food	US	BBB-	8
Kroger	KR	Food & Drug Stores	US	BBB	10
Louis Dreyfus	LOUDRE	Agri. Prod. Whslrs	NL	BBB-	14
Mars	MARS	Packaged Food	US	A	7
Marubeni	MARUB	Food & Bev. Whslrs	JP	BBB	7
McDonald's	MCD	Restaurants	US	BBB+	7
Minerva	BEEFBZ	Packaged Food	BR	BB	9
Nestle	NESNVX	Packaged Food	US	AA-	7
Nike	NKE	Apparel, Footwear	US	A+	7
Reckitt Benckiser	RKTLN	Home Products	GB	A-	7
Sodexo	SWFP	Food Services	FR	BBB+	7
Sysco	SYY	Food & Bev. Whslrs	US	BBB	6
Target	TGT	Mass Merchants	US	A	10
Tesco	TSCOLN	Food & Drug Stores	GB	BBB-	11
Tyson Foods	TSN	Packaged Food	US	BBB	10
Unilever	UNANA	Personal Care	GB	A+	5
Walmart	WMT	Food & Drug Stores	US	AA	11
Yum!	YUM	Restaurants	US	BB-	7

**ADS: AFII Deforestation Score. For full details please see "RDCP: Deforestation exposure in liquid credit portfolios", AFII, 22 Dec 2023.*

Table 2. RDCP issuance in Q2 2024 and Q3 2024. Source: Bloomberg, accessed 1 Oct 2024.

Issuer	ISIN	Pricing Date	Maturity	Currency	Size (bn)	Rating	ESG Label
RESTAURANT BRANDS INT	US68245XAT63	03-Sep-24	15-Sep-29	USD	0.5	BB	
RESTAURANT BRANDS INT	US68245XAR08	06-Jun-24	15-Jun-29	USD	1.2	BB	
CARREFOUR SA	FR001400SID8	10-Sep-24	17-Oct-32	EUR	0.75	NR	SLB
CENCOSUD SA	US15132HAJ05	22-May-24	28-May-31	USD	0.65	BBB-	
COMPASS GROUP PLC	XS2895051212	09-Sep-24	16-Sep-33	EUR	0.5	A	Sustainable
DANONE SA	FR001400SHQ2	05-Sep-24	12-Sep-31	EUR	0.7	BBB+	
DANONE SA	FR001400PU35	26-Apr-24	03-May-30	EUR	0.7	BBB+	
ELO SACA	FR001400PIA0	10-Apr-24	17-Apr-28	EUR	0.75	NR	
GENERAL MILLS INC	XS2809271047	18-Apr-24	23-Apr-34	EUR	0.5	BBB	
GENERAL MILLS INC	XS2809270072	18-Apr-24	23-Oct-30	EUR	0.5	BBB	
GLENCORE CAP FIN DAC	XS2811096267	23-Apr-24	29-Apr-31	EUR	0.6	BBB+	
KLABIN SA	BRKLBNDBS087	15-Aug-24	15-Aug-39	BRL	1.5	N.A.	
KROGER CO	US501044DW87	20-Aug-24	15-Sep-54	USD	2.1	BBB	
KROGER CO	US501044DV05	20-Aug-24	15-Sep-34	USD	2.2	BBB	
KROGER CO	US501044DX60	20-Aug-24	15-Sep-64	USD	1.5	BBB	
KROGER CO	US501044DU22	20-Aug-24	15-Sep-31	USD	1.3	BBB	
KROGER CO	US501044DT58	20-Aug-24	15-Sep-29	USD	1.4	BBB	
KROGER CO	US501044DR92	20-Aug-24	15-Aug-26	USD	1	BBB	
KROGER CO	US501044DS75	20-Aug-24	15-Aug-27	USD	1	BBB	
MARUBENI CORP	XS2900964565	10-Sep-24	19-Sep-29	USD	0.5	BBB+	
MARUBENI CORP	JP387760AQ74	12-Jul-24	19-Jul-30	JPY	15	N.A.	
MARUBENI CORP	JP387760AQ41	19-Apr-24	25-Apr-34	JPY	14	N.A.	
MCDONALD'S CORP	US58013MFX74	14-May-24	17-May-29	USD	0.5	BBB+	
MCDONALD'S CORP	CA580135CF69	14-May-24	21-May-31	CAD	1	BBB+	
MCDONALD'S CORP	US58013MFY57	14-May-24	17-May-34	USD	0.5	BBB+	
NESTLE CAPITAL CORP	XS2813325623	02-May-24	15-May-31	USD	0.175	AA-	
NESTLE CAPITAL CORP	XS2813325201	02-May-24	15-May-34	USD	0.175	AA-	
NESTLE SA	CH1344316778	30-Apr-24	30-May-40	CHF	0.33	AA-	
NESTLE SA	CH1344316752	30-Apr-24	30-May-31	CHF	0.225	AA-	
NESTLE SA	CH1344316760	30-Apr-24	30-May-34	CHF	0.48	AA-	
NESTLE SA	CH1344316745	30-Apr-24	30-Nov-28	CHF	0.2	AA-	
RECKITT BENCKISER TSY	XS2842083235	13-Jun-24	20-Jun-29	EUR	0.9	A-	
RECKITT BENCKISER TSY	XS2842083318	13-Jun-24	20-Dec-32	GBP	0.3	A-	
TARGET CORP	US87612EBS46	03-Sep-24	15-Sep-34	USD	0.75	A	
TESCO CORP TREASURY SERV	XS2824047372	15-May-24	22-May-34	GBP	0.35	BBB-	
UNILEVER CAPITAL CORP	US904764BV84	07-Aug-24	12-Aug-34	USD	1	A+	
UNILEVER CAPITAL CORP	US904764BU02	07-Aug-24	12-Aug-27	USD	0.75	A+	
UNILEVER CAPITAL CORP	XS2850585626	24-Jun-24	27-Jun-31	USD	0.17	N.A.	

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