global witness

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BANKROLLING DESTRUCTION

New Global Witness analysis shows three of the world's biggest central banks[1] have purchased millions of dollars in bonds from agribusinesses linked to deforestation and land-grabbing.

KEY FINDINGS

> The US Federal Reserve alone bought $16 million of bonds issued by the Archer-Daniels-Midland Company, Bunge Ltd Financial Corp, and Cargill, Inc.

> The Bank of England invested in an undisclosed fraction of a £150 million Cargill bond, while supervising the financial stability of other financial service firms' investments.

> The European Central Bank also bought debt issued by Bunge Finance Europe B.V.

> ADM, Bunge, and Cargill have repeatedly been linked to alleged deforestation and land-grabbing in ecosystems including the Brazilian Cerrado, a hugely biodiverse savannah and critical carbon sink.

> While the Fed's bond-buying scheme has been wound down, its investment in deforestation-risk companies sent the wrong signal to investors.

> Neither the Bank of England nor the European Central Bank have published the values of their holdings in these companies, creating a lack of transparency.

> As supervisors of the private financial sector, central banks must lead by example and adopt an explicit zero-deforestation policy as part of their approach to climate change, including divestment from all deforestation-linked bonds and greater scrutiny of the threat to financial stability posed by deforestation and biodiversity loss

INTRODUCTION

Climate change and biodiversity loss present serious risks to the stability of the global financial system. Over half the world's total GDP – $44 trillion of economic value generation –– is moderately or highly dependent on nature and its services.[2] Widespread investment in deforestation-linked businesses and activities exacerbate climate change: in 2021, tropical forest loss alone produced as many emissions as India.[3]

Central banks play a key role in the economy, from supervising financial institutions to promoting consumer protection.[4] Recent years have seen increasing pressure on these banks to use their influence to respond to the climate emergency and to make sure that their policies align with their home country's net-zero plans.[5 6 7] In order to do this, they must both limit climate risk in their own investments and portfolios, and become more responsible prudential supervisors, by setting new procedures to evaluate if private financial institutions are properly assessing and mitigating their own exposure to climate change.

Another way that central banks intervene in financial markets is by buying corporate bonds, which is a form of quantitative easing.[8] Once considered radical, central banks' bond purchasing programmes have become a staple part of central banks' toolkits after the 2008 financial crisis.[9 10] Global Witness examined such bond holdings of the US Federal Reserve's Secondary Market Corporate Credit Facility, the European Central Bank's Corporate Sector Purchase Programme, and the Bank of England's Corporate Bond Purchase Scheme, operated by its Asset Purchase Facility. Through this analysis, we lay out the banks' exposure to deforestation risks and how they must up their game to avoid contributing to climate catastrophe.

THE ROLES OF CENTRAL BANKS

Central banks' roles have expanded in recent years as their massive monetary stimuli have backstopped the global economy, first during the financial crisis of 2008, and more recently amid the global slowdown caused by the COVID-19 pandemic.[11 12] They make decisions that determine the rate at which companies and individuals can borrow money, through multi-billion-dollar interventions in financial markets.[13]

Bond purchasing programmes, like the Bank of England's Corporate Bond Purchase Scheme, can inject credit into financial markets at times when institutions in the private sector are unwilling to lend, ultimately reducing the cost of borrowing for companies whose debt they pick up and boosting overall economic activity.[14]

Palm oil is a major driver of deforestation in the tropics.
Global Witness

However, with this power comes responsibility, and our analysis raises questions about how far these bond purchases are in the public interest or align with climate concerns. For instance, the Bank of England is expected to operate "for the good of the people of the United Kingdom" – but by purchasing bonds from a deforestation-risk company, it is effectively subsidising that company by making it cheaper for it to borrow money – and indirectly enabling forest destruction.[15] And while the Bank of England owns this debt, its purchasing programme is wholly indemnified by HM Treasury.[16] That means that the Treasury covers any losses on the portfolio, using money from taxpayers who are likely to be unaware of which companies the Bank has chosen to back.

WHAT WE FOUND

New Global Witness analysis now shows that the Bank of England, European Central Bank, and the US Federal Reserve System have purchased large volumes of debt issued by companies linked to deforestation and forest destruction.

We found Cargill, a major player in the ecologically destructive Brazilian soy industry, listed in the Bank of England's database of debt holdings. The findings showed that the Bank of England purchased an undisclosed portion of a £150 million Cargill bond after the Corporate Bond Purchase Scheme's creation in 2016.[17]

Cargill has been repeatedly tied to allegations of deforestation and land-grabbing. In 2010—years before the bond purchase—Rainforest Action Network alleged the commodities giant had illegally cleared rainforest and peatlands in Indonesia.[18] (Cargill called these allegations 'categorically untrue'.[19])

Despite Cargill having pledged to end all deforestation in all commodities in its supply chain by 2020, trade groups representing the company as well as Archer-Daniels-Midland (ADM) and Bunge were found to have lobbied the EU to weaken its anti-deforestation plans in the final days of the COP26 climate conference, according to Greenpeace's Unearthed.[20] The companies said that they were committed to ending deforestation and that their lobbying was intended to suggest more effective ways of doing so.

And as recently as 2021, Cargill was caught buying soy from deforested and illegally acquired land in Brazil's Cerrado ecosystem. The company did not dispute it had purchased this soy, but reiterated that it was committed to ending deforestation in the Cerrado—while acknowledging it would not meet that 2020 target of doing so.[21]

Global Witness's findings echo research from the New Economics Foundation, a British think tank, which suggest there is a 'carbon bias' in the Bank of England's quantitative easing programme that has led to it disproportionately investing in carbon-intensive sectors including fossil fuels.[22]

Approached for comment, the Bank of England pointed Global Witness to its 2022 climate disclosure, which does not mention deforestation, but did not dispute our findings.

The Federal Reserve, meanwhile, appears to have purchased $16 million in corporate debt from a range of controversial agribusiness traders including ADM; Bunge Ltd. Financial Corp, which is wholly owned by Bunge Ltd.; and Cargill.[23]

A 2021 Global Witness investigation found that ADM, Bunge and Cargill fuelled human rights abuses by purchasing from soy suppliers in conflict with traditional communities in Brazil's Bahia state.[24] In their responses, Cargill denied some commercial relationships while not responding concretely to evidence of purchases from soy producers involved in the conflict. Bunge has repeatedly refused to confirm or deny purchasing from companies involved. ADM acknowledged it did source from some of the farmers involved, but would not confirm or deny which ones. The trader opened, then closed, a grievance without consulting the communities involved, which it reopened when Global Witness flagged it was breaking its own policy.

A separate Global Witness investigation found that nearly 40% of sampled Indonesian palm oil mills supplying ADM and Bunge have been accused of serious harms, including violating local communities' land rights; criminalising or attacking land and environmental defenders; and/or causing serious environmental degradation.[25] Bunge acknowledged these alleged offenses were in its indirect supply chain, and added that credible instances of human rights violations were added to its grievance list;

ADM disputed Global Witness's findings but said it had launched investigations into each allegedly problematic mill; these are ongoing.[26]

Bunge's soy operations in Brazil have also been linked through its supply chain to almost 17,000 forest fire alerts in 2020 and an area of deforestation risk close to four-fifths the size of Chicago in the years between 2015 and 2018, according to Chain Reaction Research and Trase Finance.[27] Bunge told Global Witness that it was "committed to reaching deforestation-free supply chains in 2025", adding, "Bunge does not source soy from illegally deforested areas and has leading traceability and monitoring data of our direct and indirect purchases."

Cattle farming is the leading driver of tropical deforestation. *Global Witness*

When approached for comment, the Fed did not dispute Global Witness's allegations, and referred us to an FAQ describing the terms of eligibility for companies to participate in its bond purchasing program, which is silent on both deforestation risk and climate risk more broadly.[28]

Meanwhile, the European Central Bank's Corporate Sector Purchase Programme, created in 2016, invested in debt issued by Bunge Finance Europe B.V., also a wholly-owned subsidiary of Bunge Limited.[29] This bond appears in the first list of holdings made available on the bank's website, from June 2017. More than five years later, as of August 2022, the bank was still holding on to this bond despite its pledge the year prior to incorporate climate change risk considerations into the criteria it uses for its corporate bond purchases.[30]

Reached for comment, an ECB spokesperson said, "[T]he Eurosystem does not publish a detailed breakdown of its corporate bond holdings by issuer. Such disclosure could compromise the effectiveness of monetary policy and impair the ECB's ability to pursue its primary objective of price stability. However, the Eurosystem remains committed to being as transparent as possible. It will therefore continue to publish breakdowns by country, rating and industry sector every six months." The bank did not address Global Witness's concerns regarding deforestation.

The decisions of central banks to purchase corporate bonds in effect reduces the costs of borrowing for these companies and sends a signal to other investors that these businesses are legitimate.[31]

At the end of last year, Global Witness showed that banks and asset managers based in EU, UK, US and China made deals worth $157 billion with firms accused of destroying tropical forest in Brazil, Southeast Asia and Africa between 2016 and 2020.[32] Global Witness's new findings mean that it's little wonder private banks and asset managers — which take their cues from the central banks — are still so heavily invested in some of the most environmentally destructive firms on the planet.

CENTRAL BANKING AND CLIMATE CHANGE: DEFORESTATION IS MISSING FROM THE AGENDA

Central banks are saying one thing about climate change and doing another by holding the bonds identified by Global Witness.

Publicly, central banks increasingly refer to climate change as both a 'physical risk', resulting in potential damage to tangible assets, like land and buildings, and a 'transition risk' that arises where businesses and the financial sector are unprepared or unable to respond to climate-related changes in regulation, technology, litigation and consumer preferences, among other factors.[33]

Deforestation carries a high level of physical and transition risk, not least because the environmental damage caused elevates the likelihood of extreme weather and global food insecurity, as well as exposing companies and their financiers to the significant financial risk posed by litigation by affected local communities. Table 1 (below) presents a full exploration of the physical and transitional risks posed by deforestation.

Measuring these climate- and nature-related risks and their potential impact on financial stability is new territory for most central banks. In 2017, eight central banks and supervisors founded the Network for Greening the Financial System (NGFS) to mobilise climate finance and develop new risk assessment and supervision methodologies.[34]

Now boasting over 116 members, in March 2022, NGFS research highlighted deforestation an issue of 'particular concern' for financial stability risks emanating from biodiversity loss.[35]

Yet despite this, deforestation is still missing in action from the central banking agenda.

At COP26, Frank Elderson, Chair of the NGFS and Vice-Chair of the Supervisory Board of the European Central Bank acknowledged 'forests – and more broadly, nature – have so far remained too much in the shadows… Forests and finance are more intricately intertwined than ever and only together they can thrive'.[36]

The Bank of England, European Central Bank, and the Federal Reserve are all members of the NGFS, but have made uneven progress on deforestation to date.[37] For the first time, both the Bank of England and the European Central Bank have issued guidance to their supervisees in the private financial sector, asking them to take a strategic approach to identifying, managing, and mitigating climate-related financial risks. Neither bank, however, has prioritised the risks posed by deforestation in this guidance.[38] [39]

They have also begun to 'stress test' the financial sector's preparedness to deal with climate risks.[40] In May 2022, the Bank of England estimated that climate change could cost UK banks more than £340 billion by 2050 if action is severely delayed, stating that the financial sector 'still need to do much more to understand and manage … exposure to climate risks'.[41] [42] None of the scenarios used in the test sought to measure exposure to biodiversity loss or deforestation specifically, however.

Unsurprisingly given the deforestation-linked bond purchases uncovered above, the Bank of England's 2020-21 annual report concluded 'the portfolio as a whole is still not on track to meet climate goals'.[43] In November 2021, it committed to 'greening' its corporate bond buying programme, supporting the UK government's ambitions to be the world's first net-zero financial centre, but failed to mention the need to divest from deforestation.[44 45]

The Bank announced that "in light of economic conditions" it would begin sales of its corporate bond holdings, including Cargill, in September 2022.[46 47]

Client Earth recently reported that the European Central Bank's debt from high-emitting companies makes up more than half of the $266 billion of assets held under the bank's corporate bond buying scheme.[48]

Rapid changes are required to decarbonise public and private portfolios alike. The European Central Bank's climate stress test of private European banks, published in July 2022, concluded 'most [Euro Zone] banks do not include climate risk in their credit risk models, and just 20% consider climate risk as a variable when granting loans'.[49]

The Federal Reserve, by comparison, has lagged even further behind until now. In October 2021, the U.S. Financial Stability Oversight Council, whose members include the Federal Reserve Chairman, published a report in response to President Biden's Executive Order 14030 on *Climate-Related Financial Risk.*[50 51] This acknowledged recent steps taken by the Fed to incorporate climate-related financial risks into its supervision of financial firms, while calling for further actions by its members to address the "emerging threat to financial stability caused by climate change'.[52]

The same report acknowledged deforestation to be a 'driver' of physical risk, with the Commodity Futures Trading Commission identifying agribusinesses as highly exposed from a physical or transitional perspective too.[53]

By September 2021, the Federal Reserve had wound down its corporate bond program, selling all the bonds it held through the facility invested in ADM, Bunge, and Cargill.[54] But these sales were in response to improved credit flow, not concerns about the risk posed by deforestation.[55] This leaves the door open for the bank to invest in deforestation-risk industries in the future.

Lael Brainard, the Fed's Vice Chair as of May 2022, has indicated the bank will begin stress testing US financial institutions on climate grounds in the future, 'actively learning' from the European and Bank of England process.[56 57] Global Witness urges that this include an evaluation of the exposure of the bank itself and the private institutions it supervises to deforestation and associated land degradation.

The US Securities and Exchange Commission (SEC) has also proposed rule changes that, if adopted, would require public companies to provide detailed reporting of their climate-related risks and emissions.[58] If designed and implemented correctly, this new rule could see companies reporting on their exposure to deforestation.

THE WAY FORWARD FOR CENTRAL BANKS

Although central banks play a politically 'independent' role, they do not operate in a vacuum. The 2008 financial crash and Covid-19 pandemic has demonstrated their willingness to take extraordinary measures in the name of long-term financial and monetary stability.

To combat rising inflation, central banks are now reducing their balance sheets, selling off the corporate bonds they bought to steady the global economy during the Covid-19 pandemic. The Federal Reserve and Bank of England have already begun or completed this process, while economists think that the European Central Bank will be slower to wind down its asset purchases, potentially delaying into 2023.[59]

While this divestment from deforestation-risk companies from central banks is welcomed, it should be noted that these sales are predominantly driven by concerns about inflation, not a concerted effort to root out the financing of deforestation and associated human rights abuses from central bank portfolios.

In 2021, tropical forest loss alone produced as many emissions as India. *Global Witness.*

Plus, selling off the deforestation-linked bonds mentioned in this report merely displaces, but does not eliminate, the climate risk these companies pose. As supervisors, central banks must also make it clear that private investors should avoid the significant risk that comes with buying high-risk agribusiness corporate bonds. For the Bank of England, this would be in keeping their strategy to 'incentivise firms to take decisive actions that support an orderly transition to net zero'.[60]

One way to nudge the market is for central banks to publicly commit to not purchasing deforestation-risk bonds in the future as part of their approach to climate change. This can be easily achieved by conducting due diligence to screen out high deforestation-risk industries and sectors. For example, the Swiss National Bank – the country's central bank – does not invest in companies whose products 'seriously violate fundamental human rights'. In 2020, the bank said it would also exclude companies whose productions 'seriously damage biodiversity'.[61]

The European Central Bank and Bank of England have agreed to gradually decarbonise their corporate bond holdings to meet the objectives of the Paris Agreement by incorporating climate-related factors in their decision making. The Bank of England said it will no longer buy bonds issued by companies in high-emitting sectors such as energy and utilities unless they have published decarbonsation targets.[62] From October 2022 the European Central Bank will base its bond purchases on good climate performance, among other factors.[63] Company performance related to biodiversity loss is not well reflected in these new investment frameworks, however.

As the formation of the NGFS signals, only a universal approach to assessment, disclosure and mitigation will work. As a result, central banks must adopt clear, consistent and transparent strategy to address deforestation and associated human rights abuses.

Future climate 'stress test' exercises must also see central banks require that their supervisees pay specific attention to deforestation risks in their portfolios. Central banks in the Netherlands, France, Mexico and Malaysia have all conducted assessments into risk exposure associated with biodiversity loss.[64] Others must now follow suit.

Credit rating agencies also have a role to play. These powerful agencies influence investor behaviour by assessing the risk of investments, but Global Witness has shown that they have ignored deforestation in producing these ratings in the past.[65 66] Credit rating agencies should take note of the outcomes of these stress test exercises, adapting their products to factor in the true carbon cost of the land and agricultural sector.

REGULATION IS ESSENTIAL

Yet central banks cannot solve our global deforestation crisis alone. Aligning financial flows to end deforestation – as already pledged by US, UK and key European governments at the COP26 summit in Glasgow[67] – will require coordination between governments, central banks and the private sector.

Governments hold the most powerful tools required to push through a green transition, namely laws, regulations, taxes and subsidies.[68]

The financial sector has so far pointed to its voluntary commitments, including internal policies and public commitments, to address financiers' links to deforestation. But this has proved completely inadequate. Twelve major banks signed up to the 'Soft Commodities Compact' on deforestation in 2014 to achieve zero-net deforestation by 2020, which has clearly failed to deliver.[69] Companies such as meat-giant JBS still attract significant investment from members of that scheme despite well documented environmental and human rights harms.[70] This failure has meant that continued high rates of deforestation globally are putting at risk whole ecosystems, proving disastrous for local communities, as well as the global climate.[71]

Regulators and legislators must therefore move quickly to stop the financing of deforestation by all market actors.

The UK's upcoming revisions to its financial regulation framework,[72] an incoming EU law on deforestation[73] and a recent forest-focussed Executive Order[74] issued by the Biden Administration offer renewed opportunities to legislate against the financing of deforestation, but only if action is taken now. Too many opportunities have been missed already whilst the world's forests are being destroyed at a rapid pace.

Given the rate at which the financial system needs to decarbonise, if we are to have any chance of keeping global heating below 1.5 degrees Celsius, legislators and the key banks – central and private – must take urgent action on deforestation.

In summary, this report recommends:

> Central banks should divest from all deforestation-linked corporate bonds.

> Central banks should adopt an explicit zero-deforestation policy as part of their climate, nature, and biodiversity strategies, conducting due diligence on new investments and reporting on deforestation as part of their nature-related disclosure obligations.

> Central banks should assess the private financial sector's exposure to deforestation and agribusiness risk alongside other carbon intensive industries as part of their climate-related prudential supervision activities, including in 'stress test' exercises.

> Governments must effectively regulate financial institutions and companies to halt and prevent the financing of deforestation, empowering central banks to execute their prudential supervision role effectively.

METHODOLOGY

Global Witness compared corporate sector bond holdings by the European Central Bank, the Bank of England, and the US Federal Reserve System with the list of companies observed by Forests & Finance, which assesses the financing of over 300 companies producing select commodities (including beef, soy, and palm oil) whose operations may impact tropical forests in Southeast Asia, Central and West Africa, and parts of South America. This analysis may therefore exclude similar companies with impacts on other tropical forests, or temperate forests. We excluded some findings where we deemed allegations of deforestation or logging against a company to be insufficiently substantiated, out of date, or both.

We examined publicly available lists of bond holdings of the European Central Bank's Corporate Sector Purchase Programme, which was created in 2016, between 23rd June 2017 - 4th February 2022. For the Bank of England, we analysed publicly available data containing its list of bond holdings under the Corporate Bond Purchase Scheme, which became operational in 2016. To analyse bond investments by the US Federal Reserve through its Secondary Market Corporate Credit Facility, which was created in 2020, we checked SMCCF Transaction Specific Disclosures to identify companies of interest.

PHYSICAL RISKS	PRACTICAL EXAMPLES
Greenhouse emissions from deforestation increase global temperature rises Deforestation and land degradation result in lost carbon sinks	An estimated 11% of global greenhouse gas emissions come from deforestation and forest degradation, which contributes to global temperature rises.[75] Forests provide a "carbon sink" that absorbs a net 7.6 billion metric tonnes of CO2 per year, 1.5 times more carbon than the United States emits annually.[76]
Extreme weather	Deforestation in the Amazon changes precipitation patterns across South America, jeopardising agricultural yields and more.[77]
Threat to local and global ecosystem services Soil erosion caused by deforestation increases global food insecurity	According to IUCN, 52% percent of all land used for food production is already moderately or severely impacted by the erosion of healthy soil. This occurs when trees are removed from a landscape, leading to increased food insecurity.[78]
TRANSITION RISKS	**PRACTICAL EXAMPLES**
Changing consumer preferences result in severely decreased market opportunity for forest-risk commodities	In 2020, 230 investors with $16.2 trillion assets under management (AUM) asked hundreds of companies to either meet their commodities supply chain deforestation commitments or risk economic consequences. The letter outlines that "[c]onsidering increasing deforestation rates and recent fires in the Amazon, we are concerned that companies exposed to potential deforestation in their Brazilian operations and supply chains will face increasing difficulty accessing international markets".[79]
Litigation against agribusinesses and their funders based on evidence of human rights abuse and illegal deforestation significantly decreases their market value.[80]	In 2020, the Australia and New Zealand Banking Group repaid Cambodian victims the profits it had made from an estimated $40 million loan to

	an alleged land-grabbing sugar company nine years earlier.[81]
Failure or inability to comply with incoming supply chain legislation results in inability to sell to key markets, or direct penalties and sanctions.[82] [83] Changing regulations make the financing of all deforestation illegal, undermining company business models that routinely rely on deforestation.[84] Binding National 'green investment taxonomies' explicitly exclude investment in deforestation-linked industries or businesses, increasing the risk of stranded assets.[85]	**EU and UK**: New supply chain due diligence obligations in the European Union and the UK will require businesses to prove their products and services are deforestation-free, which could negatively impact global businesses if they are not prepared or cannot or have not developed the resources to do so.[86] [87] **US**: In 2021, bipartisan support saw the introduction of the Fostering Overseas Rule of Law and Environmentally Sound Trade (FOREST) Act, which seeks to eliminate illegal deforestation by prohibiting the U.S. importation of products made wholly or in part of certain commodities produced on illegally deforested land.[88]

Table 1. Examples of the physical and transition risks posed by deforestation to the financial sector. Analysis adapted from *Niamh McCarthy, Matt Piotrowski, 'Climate-Related Forest, Food, and Land Risks Threaten US Financial Stability', 2022*.

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