

How we're tackling Brazilian deforestation

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Forest fires are harming both Brazil's environment and its sovereign investment credibility. As bondholders, we're taking action and driving engagement with policymakers to help preserve the country's unique rainforest resource, which in turn supports its creditworthiness.

Images of burning Brazilian rainforest make for a shocking scene. At the environmental level, combating forest fires is one part of a global push to tackle climate change and the devastating impacts it is having on our planet.

None of us are immune to the ethical and environmental implications, but investors face a third issue – financial risk.

Biodiversity and climate change represent potential systemic risks that can impact a country's creditworthiness. In our view, high and increasing deforestation rates are not only making Brazil less appealing as a sovereign investment on ESG grounds given the critical role they play in providing ecosystems and regulating the climate, they are also impacting its ability to harness its forestry assets in the future for positive

sustainability and finance initiatives, such as carbon financing, as well as in meeting its climate change obligations set out in the Paris Agreement.

With ESG considerations embedded throughout our investment process, increased deforestation is becoming both an environmental issue and a credit concern for us as long-term sovereign bond investors for those countries where this is a material issue. Ultimately, forest fires degrade Brazil's creditworthiness and will likely cause deterioration in the price of its assets.

In June, we began taking action, working with 29 other investors with a total AuM of USD3.7 trillion to raise the issue with Brazilian embassy representatives in many countries.

In the world of investor stewardship activities, our equity peers often hold an edge when engaging with corporates, of which they are shareholders. But as established fixed income investors operating in the sovereign space, we were well placed to have our message heard by the right people. The outcome was an audience with the central bank, with which we have interacted previously on monetary policy issues, then as part of the wider investor group, contact with Brazil's vice president, who leads the taskforce on deforestation in the Amazon, as well as members of the Brazilian Congress over the summer months.

Ourselves and the investor group are confident that we've got our message across and we are formalising a working group around this initiative, which will be known as the Investors' Policy Dialogue on Deforestation and co-chaired by us.

The investor coalition has set out the following five outcomes:

- 1. A significant reduction in deforestation rates, i.e. showing credible efforts to comply with the commitment set down in Brazil's Climate Law, article 19.**
- 2. The enforcement of Brazil's Forest Code.**
- 3. The ability of Brazil's agencies tasked with enforcing environmental and human rights legislation to carry out their mandates effectively and any legislative developments that may impact forest protection.**
- 4. Prevention of fires in or near forest areas, in order to avoid a repetition of the fires seen in 2019.**
- 5. Public access to data on deforestation, forest cover, tenure and traceability of commodity supply chains.**

Recognising engagement takes time and the issues and dynamics are complex and multi-dimensional, the investor initiative has agreed on an initial two-year programme of dialogue. We hope it will set the model for future proactive investment-relevant ESG initiatives with other sovereigns.

Reflecting on our knowledge and insights of the sovereign, while the messaging from the top isn't always conducive to our efforts on matters of the environment and deforestation, we are encouraged that it doesn't run through the entire government. Indeed, there are many strands of opinion within it – some departments clearly appreciate the severity of the issue and are working hard to address it. We might differ over the best approaches and solutions to do this, but the underlying impetus to preserve the rainforest is there. As such, we believe it is a case of identifying the right pressure points and working with the right people to move policy in a positive direction – as the political will exists – we believe there is scope to succeed here.

To learn more about our approach to ESG and other industry participation initiatives, [click here](#).

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