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The Failings of BlackRock's Palm Oil Engagement Approach

In May 2019, BlackRock, the $6.5 trillion asset manager, quietly released a statement on its approach to engagement with the palm oil industry. BlackRock's two-page statement came after repeated efforts to draw BlackRock's attention to its role as one of the largest investors in palm oil companies responsible for massive social and environmental impacts, including rampant deforestation, land grabbing, and human rights abuses.

This is the first time that BlackRock has provided a window into its engagement on deforestation and related human rights and sustainability issues. As such, it is a welcome illustration of BlackRock's recognition of the problems facing its palm oil investees. However, BlackRock's statement does little to illuminate the firm's engagement approach, and does much to rationalize the firm's failure to take meaningful action. BlackRock is among the largest investors worldwide in forest-risk commodities such as palm oil; but rather than effectively addressing the risks, the company has chosen to increase its holdings in conflict palm oil, while rationalizing away its opportunities to mitigate these risks.

The statement reveals the following major shortcomings, which are further elaborated below:

- It fails to acknowledge the real risks of the palm oil sector;
- It demonstrates deceptive and disingenuous stakeholder engagement;
- It demonstrates corporate engagement absent of results;
- It uses passive index construction as cover to absolve itself of its fiduciary duty;
- It provides no rationale for the fact that BlackRock's stake in the palm oil sector is increasing.

1. **Failure to acknowledge the real risks of the sector.**

This is the first time BlackRock has provided a window into its engagement on deforestation; the statement is clearly the result of a pointed letter from the US Senate, protests at BlackRock offices, and tens of thousands of petitions regarding its financing of the palm oil industry, all of which occurred shortly prior to the statement's release. In its statement, BlackRock emphasizes that "regulatory measures and shifts in consumer demand may present risks to the long-term sustainability of companies" in the palm oil sector; however it fails to acknowledge the direct material risks as well as the real impacts of massive land conversion, biodiversity loss, and human rights abuses that are inherent to the palm oil business. **BlackRock should clearly articulate a risk management approach capable of addressing the material risks of investing in this implicitly destructive sector.**

2. **Deceptive and disingenuous stakeholder engagement.**

In its Q1 2019 quarterly report BlackRock says it engaged with WWF as part of its due diligence around the palm oil sector. BlackRock did not, however, engage with other civil society groups who have raised serious concerns over its palm oil investments, including Friends of the Earth and grassroots Liberian and Indonesian organizations that have been at the forefront of palm oil expansion. By working with one civil society group, BlackRock checks the box for civil society engagement – and avoids substantive discussion with the organizations directly engaged with the issues at hand. As one example of poor stakeholder relations, BlackRock has not yet responded to this letter by Liberian human rights attorney Alfred Brownell.
BlackRock should respond to Professor Brownell, meet with civil society organizations to discuss real benchmarks for progress, and open a pathway for dialogue with directly affected communities.

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3. Engagement without results.

BlackRock says it "will continue to engage with palm oil producers, downstream buyers, and other relevant stakeholders to promote sustainable palm oil practices, as part of fulfilling our fiduciary duty." That BlackRock recognizes engagement as part of its fiduciary duty is not insignificant. But the question regarding engagement is, *to what end?* And, when BlackRock says "Companies seeking to appropriately manage the inherent risks and opportunities may require time," the question is, *how much time?*

BlackRock reveals that it has engaged with "three Indonesian, two Malaysian, one Korean, and one Liberian palm oil producer(s)." BlackRock notes that "While most of these companies are members of the Roundtable on Sustainable Palm Oil (RSPO) and have publicly committed to various traceability and certification targets, we learned through our engagements that *progress towards full compliance of standards and procedures for certified sustainable palm oil remains a challenge for the industry."* This constitutes an acknowledgment of failure to comply with the most basic standards of sustainable business; yet even this assessment is drastically understated, as these companies' practices have not only faced "challenges," – *they have gone from bad to worse.* Looking at three companies we can say with confidence are on BlackRock's engagement list, one – Indofood Sukses Makmur – was dropped by Citibank for intractable labor abuses; a second – Sinar Mas – recently had several of its executives arrested for bribery in Indonesia; and a third – Golden Veroleum Liberia – allegedly continues to clear land on its Liberian concession in violation of a formal request by the Roundtable on Sustainable Palm Oil. **BlackRock should apply time-bound, results-based engagement, and disclose how it measures progress. When engagement fails to shift companies' practices within a defined time-frame, BlackRock should vote against poor governance or phase out investments in this high-risk sector.**

4. **BlackRock repeats an assertion that asset managers regularly use to provide cover for poor fiduciary practices, when it writes, "**Third party index providers determine the companies included in a particular index. Investors cannot selectively divest companies from an index fund." While it is true that index providers play a key role in choosing the companies that BlackRock and other firms include in the portfolios they offer, it is not true that BlackRock and other firms have no control over what these funds contain. BlackRock is a $6.5 trillion asset managers, and the largest client of MSCI, which provides the bulk of BlackRock's indices. While index funds do have to closely track indices, they do not have to exactly match them. Therefore, simply put, BlackRock has the power to ask MSCI or any other index provider to construct indices that meet real sustainability criteria. The only way to de-risk a portfolio is to remove high-risk securities. **BlackRock should ask its index providers to remove poorly governed high-risk companies from indices tracked by its funds, beginning with funds marketed as sustainable; and should ask index providers to construct indices with rigorous ESG criteria to phase out exposure to problem companies and sectors.**

5. **BlackRock is increasing – not decreasing – its stake in deforestation.**

According to an analysis from first quarter 2019, BlackRock's investments in the palm oil sector have been increasing, not decreasing. This is true both in terms of the number of securities and the number shares of these securities held in BlackRock's passive funds. Even as the sector has shown that it cannot achieve true sustainability, BlackRock is increasing its stake. With only a decade left to reverse course on climate change, there is no justification for increased investment in a sector that is driving environmental destruction and human rights abuses. **Given the sector's inability to resolve its fundamental failings, BlackRock should**

provide its beneficiaries with a clear rationale for increasing its holdings in the palm oil industry, and should stringently define standards for index providers to prevent exposure to the material risks palm oil poses.

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