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Agribusiness Risks for the Responsible Investor – Food and Timber Sectors



riaa

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Innovative financing for sustainability



PRI

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Food, soft commodities and inflation is a massive emerging topic, which cannot be done justice in 15 minutes!

Instead 'snippets' on:

- ESG issues facing food and timber sectors
- ESG issues driving food inflation and prospects out to 2050
- ESG research as a proxy for management quality
- Case study of link between ESG issues and share price performance

Traditional or known issues and their management are critical

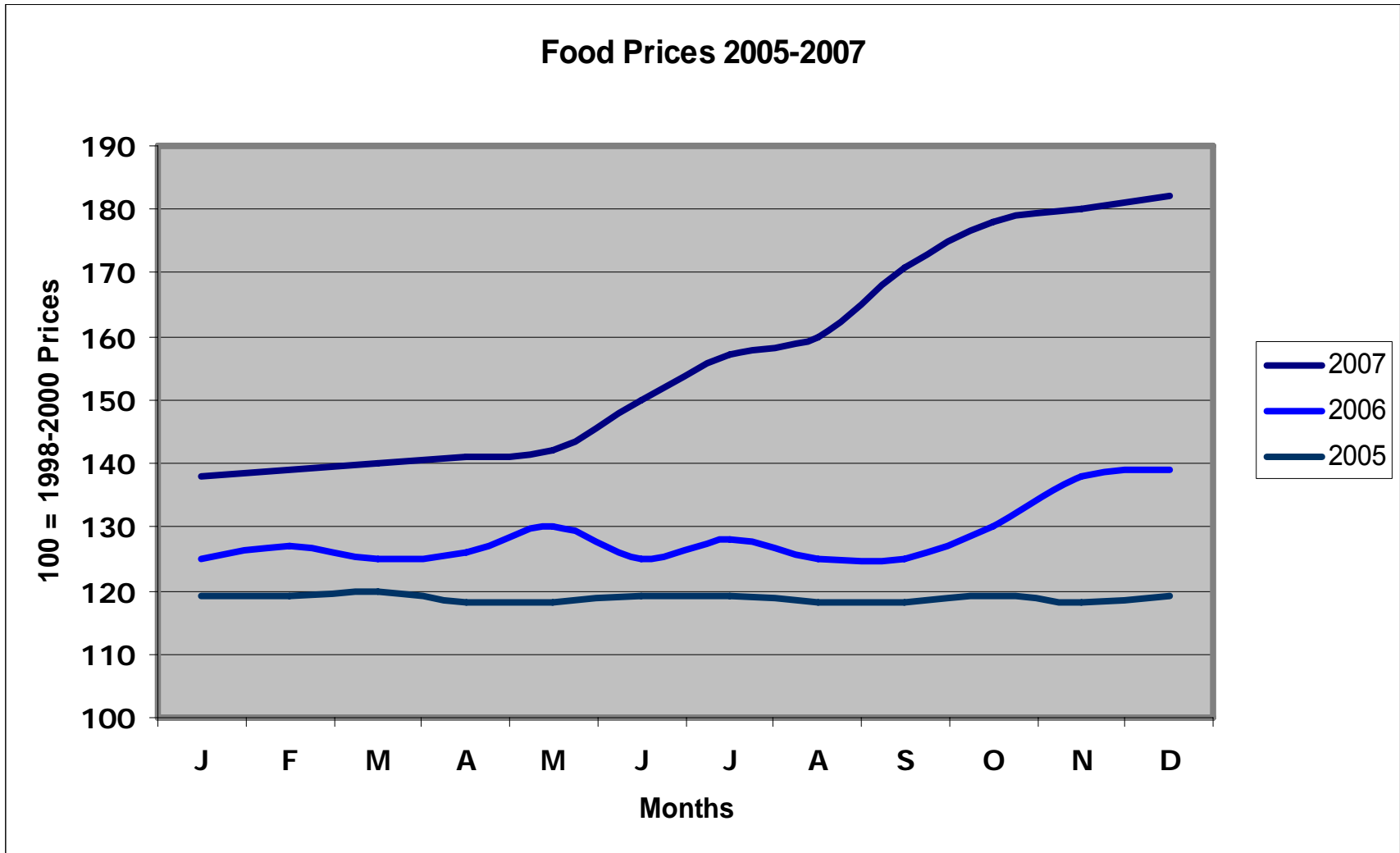
- Reengineered food/functional food/nanotechnology
- Globalization of agriculture & human rights
- Obesity/health concerns
- Food safety

Key traditional ESG issues that we evaluate:

- a) Environmental/resource management
- b) Organics/healthy eating Options
- c) Labor Rights/Strategy
- d) Food Safety Assurance
- e) GMOs/Neutraceuticals
- f) High Risks Business Activity (meat packing, biofuels, sugar)

Rising Food Prices - the New Industry Driver

Emerging market demand; competition from biofuels; climate change are driving increase in food prices – 40% in 2007



Source: Food and Agricultural Organisation, UN

Agriculture's Equivalent to the UN Intergovernmental Panel on Climate Change

1. Agri revolution of the 1960s – ↑2x world cereal production; ↑ 150% yields
2. Benefits not evenly spread globally
3. Environmental Degradation
 - 1.9bn ha & 2.6bn bn people impacted by land degradation
 - 3x more water extracted today than 50 years ago; 70% of freshwater extraction for agriculture → salinisation concerns
 - 1.6bn people live in water scarce basins
 - Agriculture: 60% methane & 50% nitrous oxide GHG emissions
 - Over fertilisation → algal blooms and eutrophication
4. 'Vicious cycle' – poor small farmers moved on to marginal land → ↑ deforestation and ↑ degradation
5. Agriculture is complex and 'multifunctional' – 'food sovereignty', 'food security'; trade and tariffs → GMOs and other transgenics may not be the answer

* IAASTD – International Assessment of Agricultural Knowledge, Science and Technology for Development – Summary for Governments; April 2008

Projections out to 2050

1. 75%↑ in global demand for cereals - of which 75% will be from emerging markets
 2. Food supply limited due to trade issues; climate change; water and land scarcity
- Innovest Interpretation:
 - Long term soft commodity and food based inflation – with short term fluctuations
 - Similar factors at play to current resources boom (Asian demand) but exacerbated by ESG issues
 - End of ‘cheap food’ akin to end of cheap oil
 - Opportunities for food and agriculture - soil and biomass for carbon capture; reduce methane and nitrous oxide emissions; decrease use of inorganic fertilisers

- Food companies are generally dealing with ‘traditional ESG’ risks poorly and are exposed to operational, litigation, reputation risks plus regulatory change
 - Recent product recalls: Archer Daniels; Tyson; Maple Leaf Food and Fonterra
 - ASX food companies generally perform poorly
 - Group Danone considered best – some energy/CO2/water/waste reductions; culturally sensitive introduction into emerging markets esp. India and Asia.
- No food company is at all well prepared for the new ESG risk - emerging soft commodity inflation
- Areas of strategic advantage become a risk, reinforcing the problem
 - 21% of companies have invested in ‘crops for fuel’ divisions influenced by regulation
 - Consumer backlash against bottled water divisions
- Opportunities found up the food supply chain - chemical companies
 - Cellulosic and biomass: 3rd generation ethanol and biofuels

Applying Innovest's Four Pillars of Intangible Value

1. Environment:

- Sustainable forestry/ certification
- Resource scarcity and plantations
- Environmental Risk Management
- Emerging value of forests as carbon sinks

2. Stakeholder Management:

- Policy makers
- Local Communities / NGO's - majority support wilderness preservation

3. Strategic Governance:

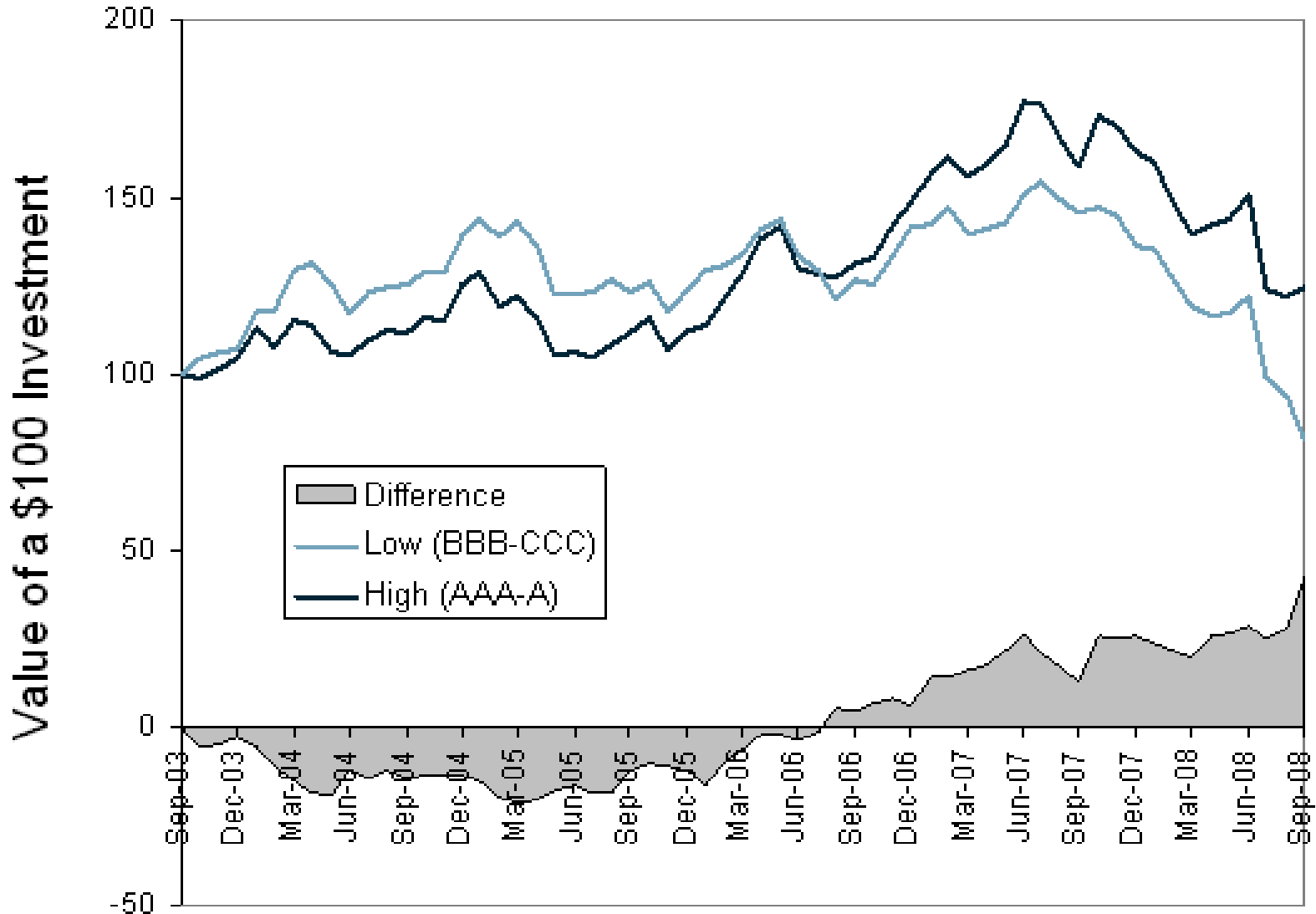
- Traditional Governance
- Strategic capability /adaptability - the multiple 'values' of forests

4. Human Capital

- Labour relations versus cost management
- Employee motivation and managing downturns

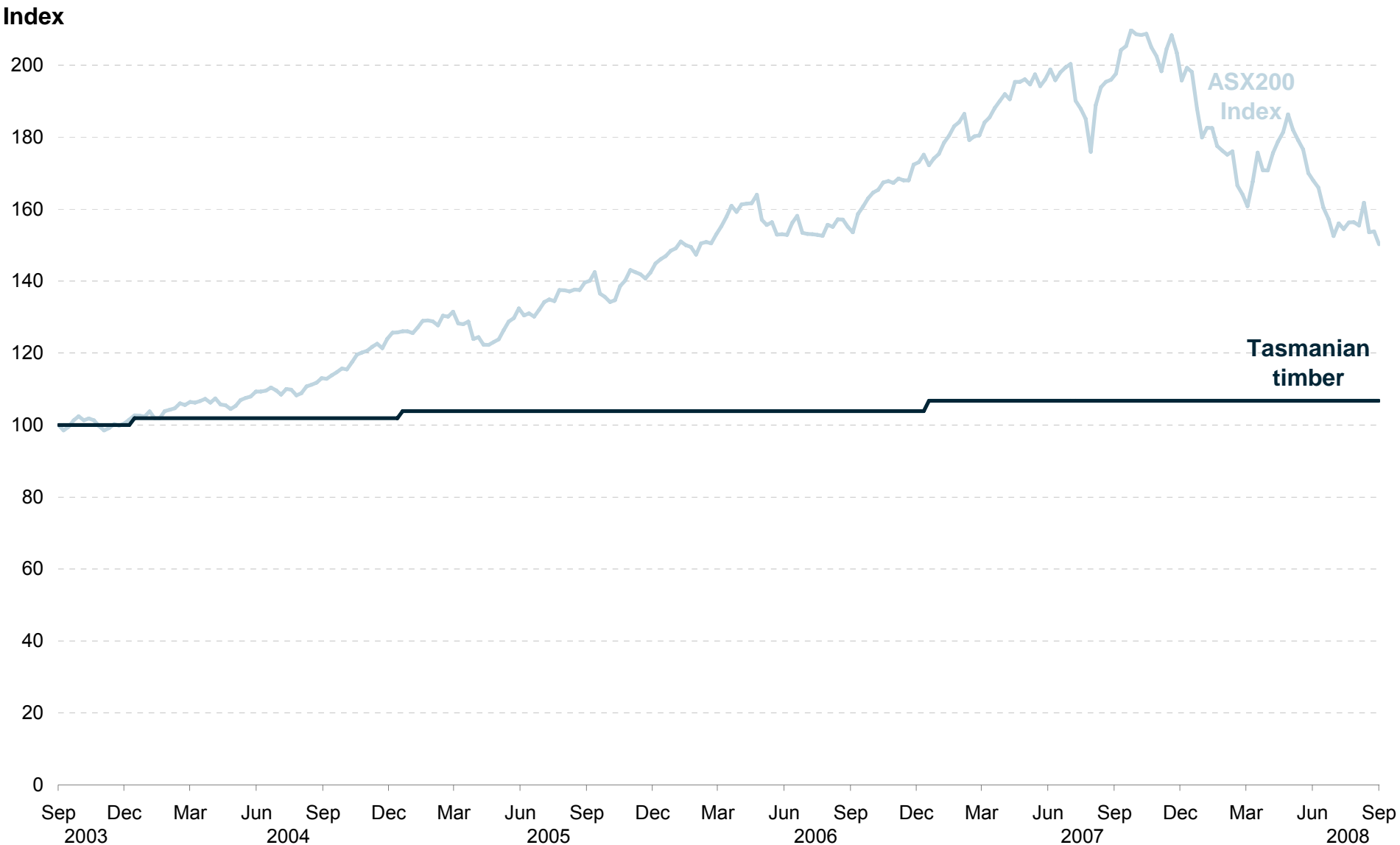
Good ESG management = Good Share Price Performance

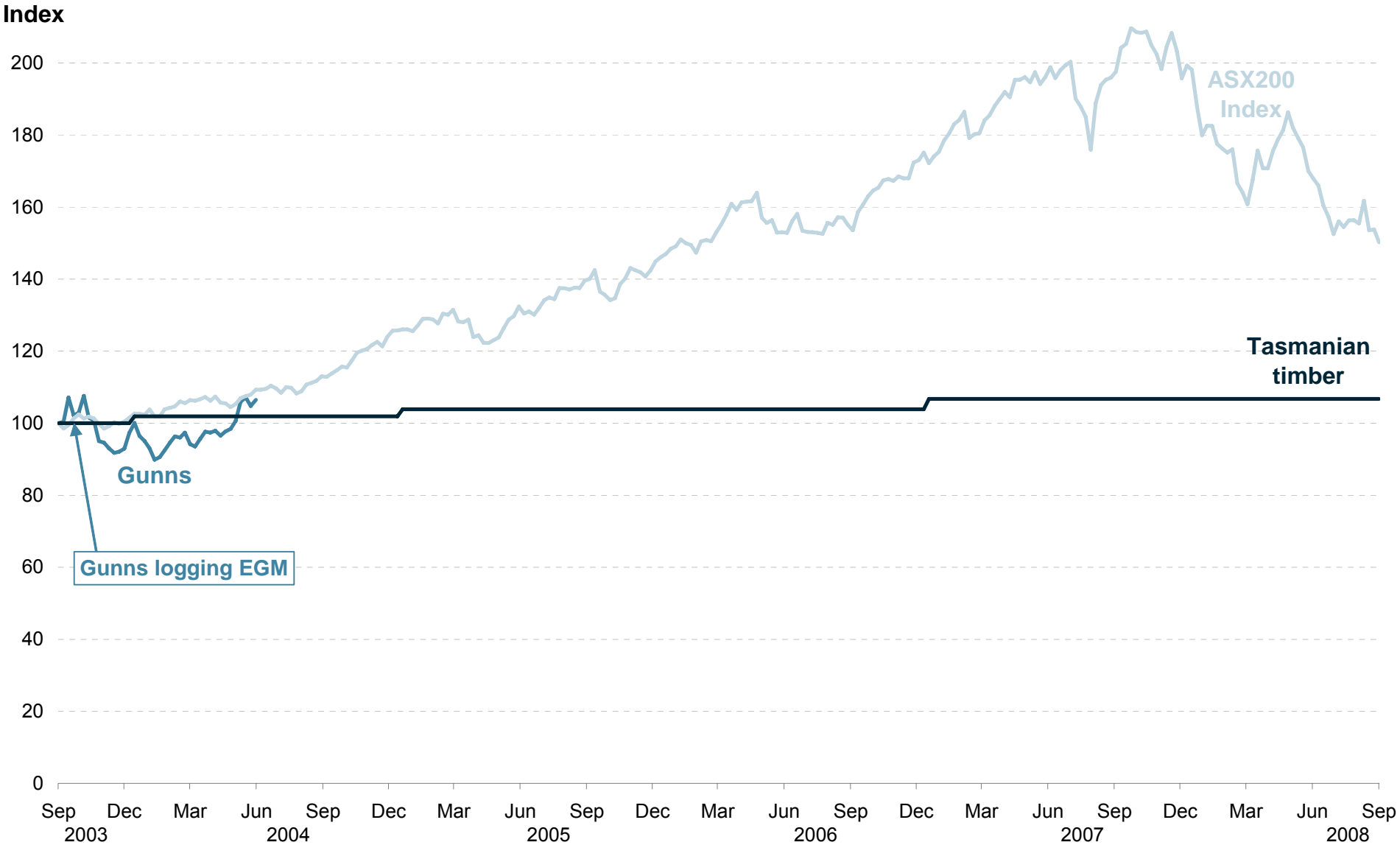
Forestry – Share price performance ESG leaders v laggards



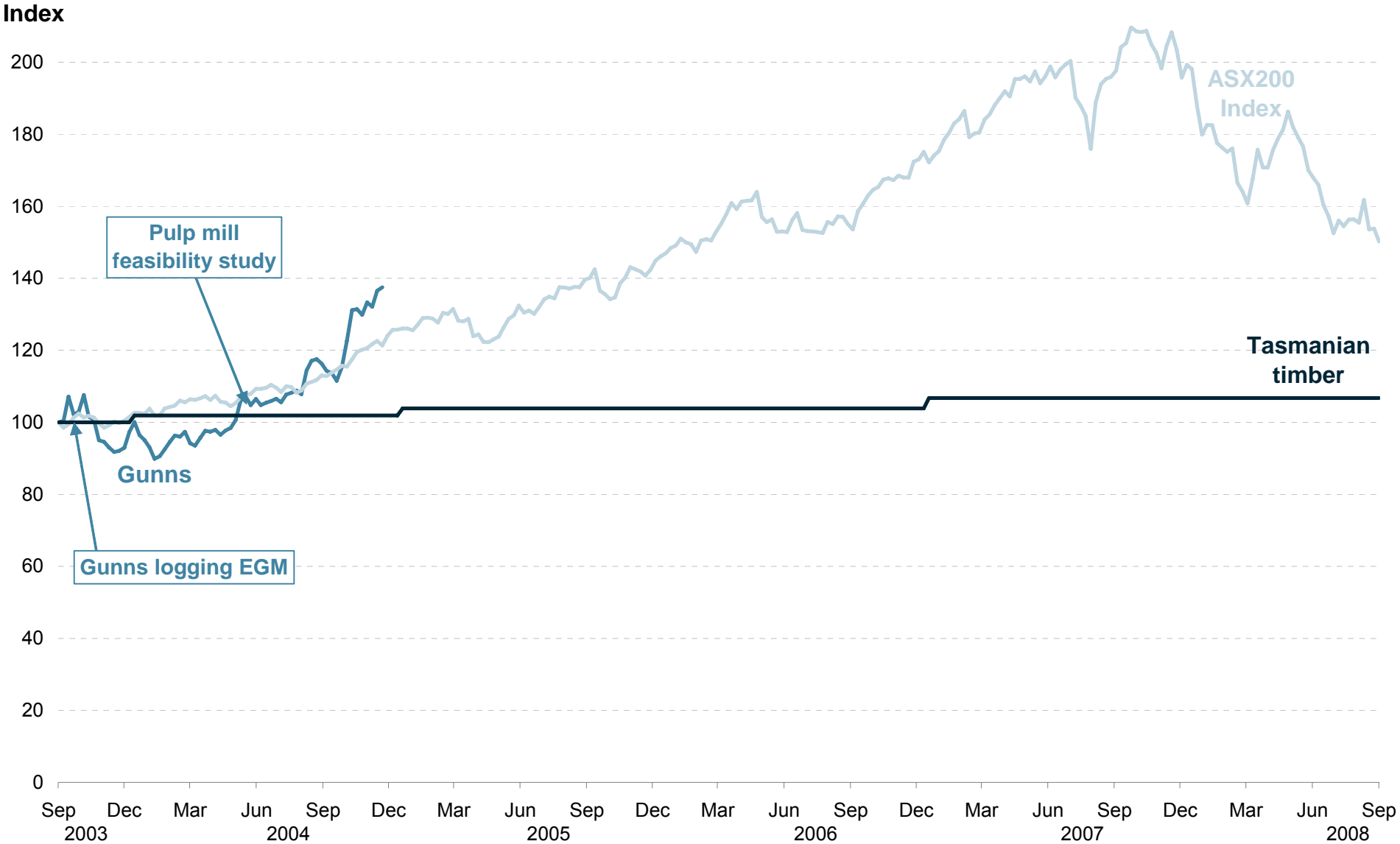
Source: Innovest

Timber is a soft commodity too. To date has underperformed the ASX

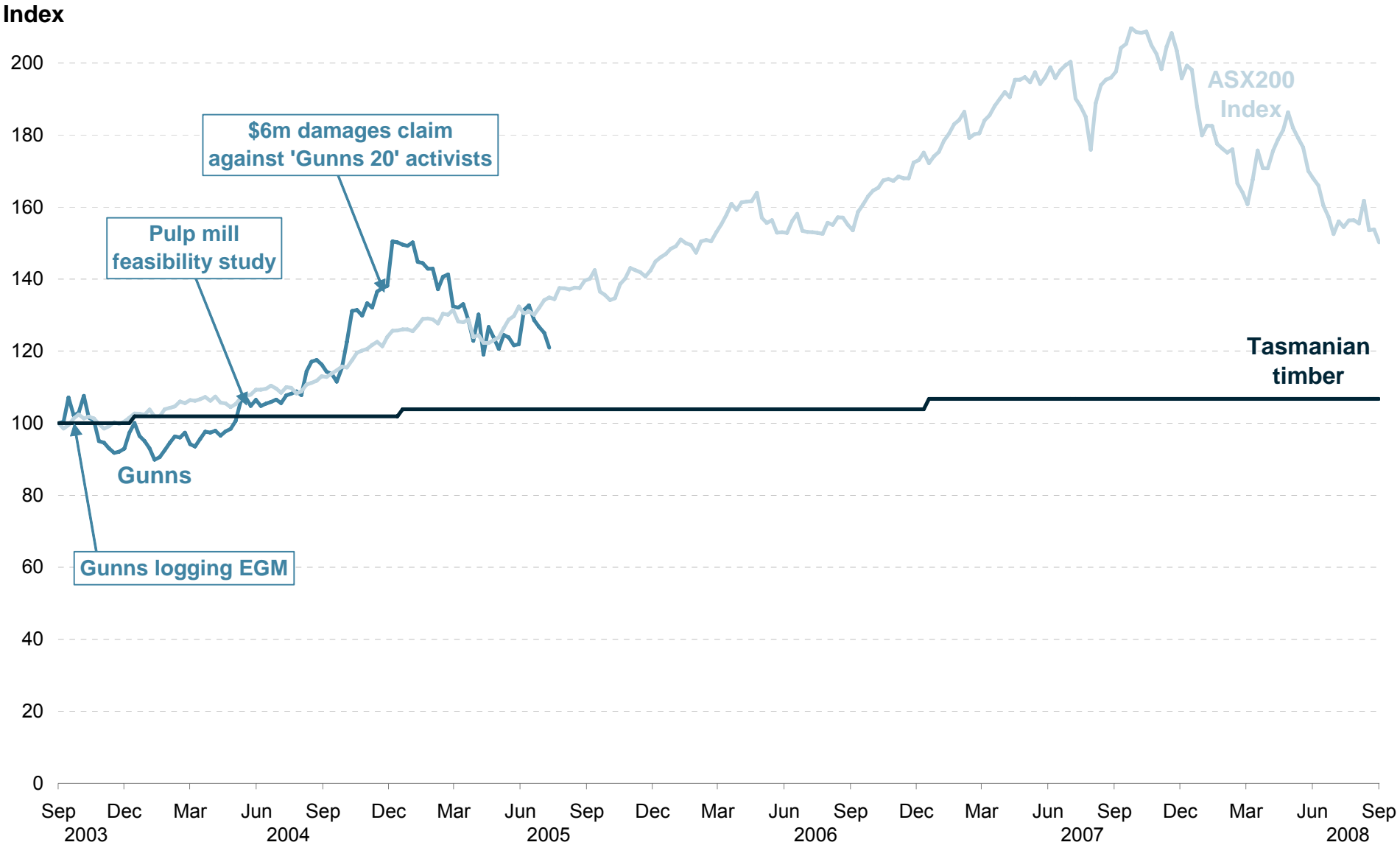




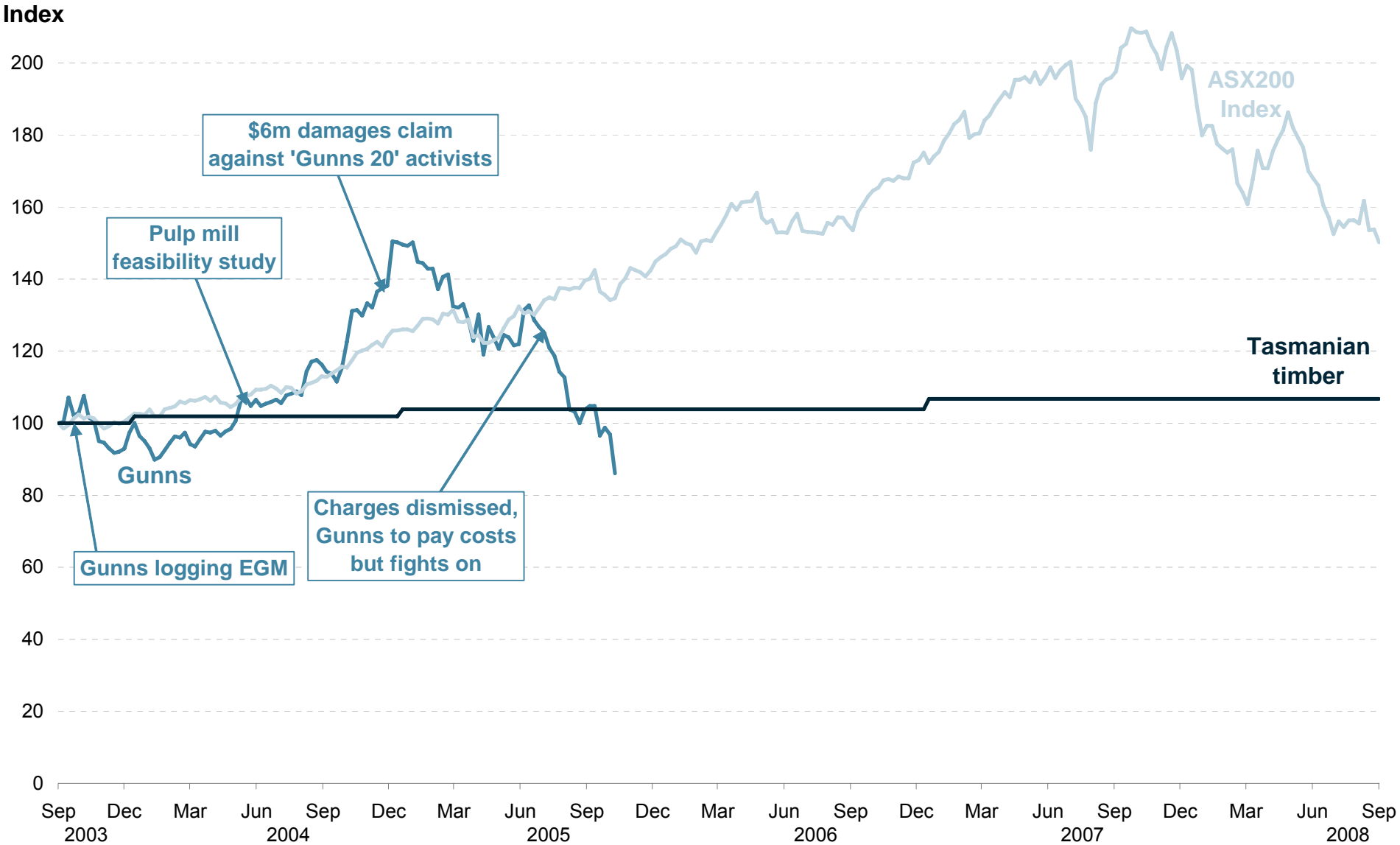
Gunns – Pulp mill gives growth strategy



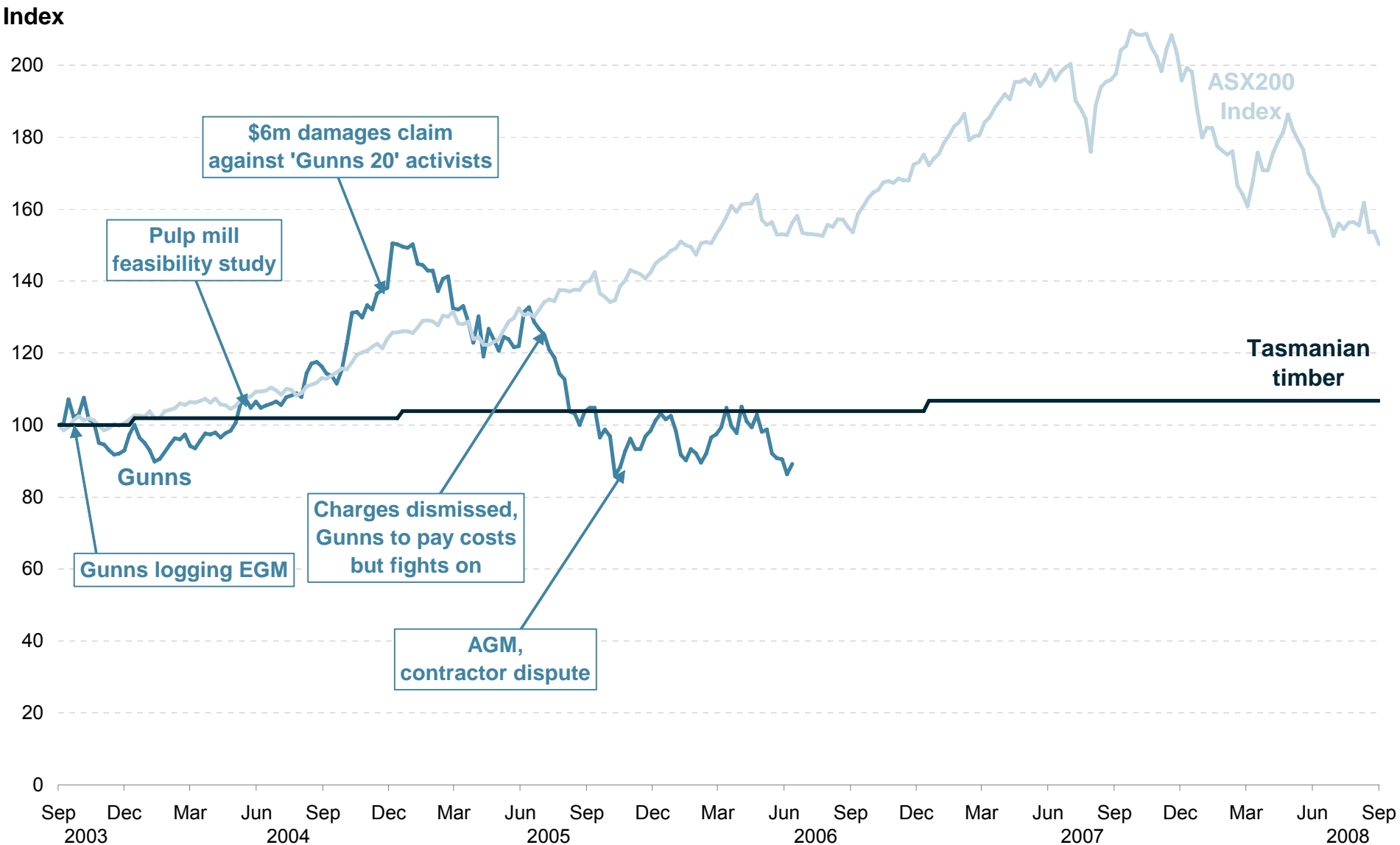
Gunns – Stakeholder relations tested



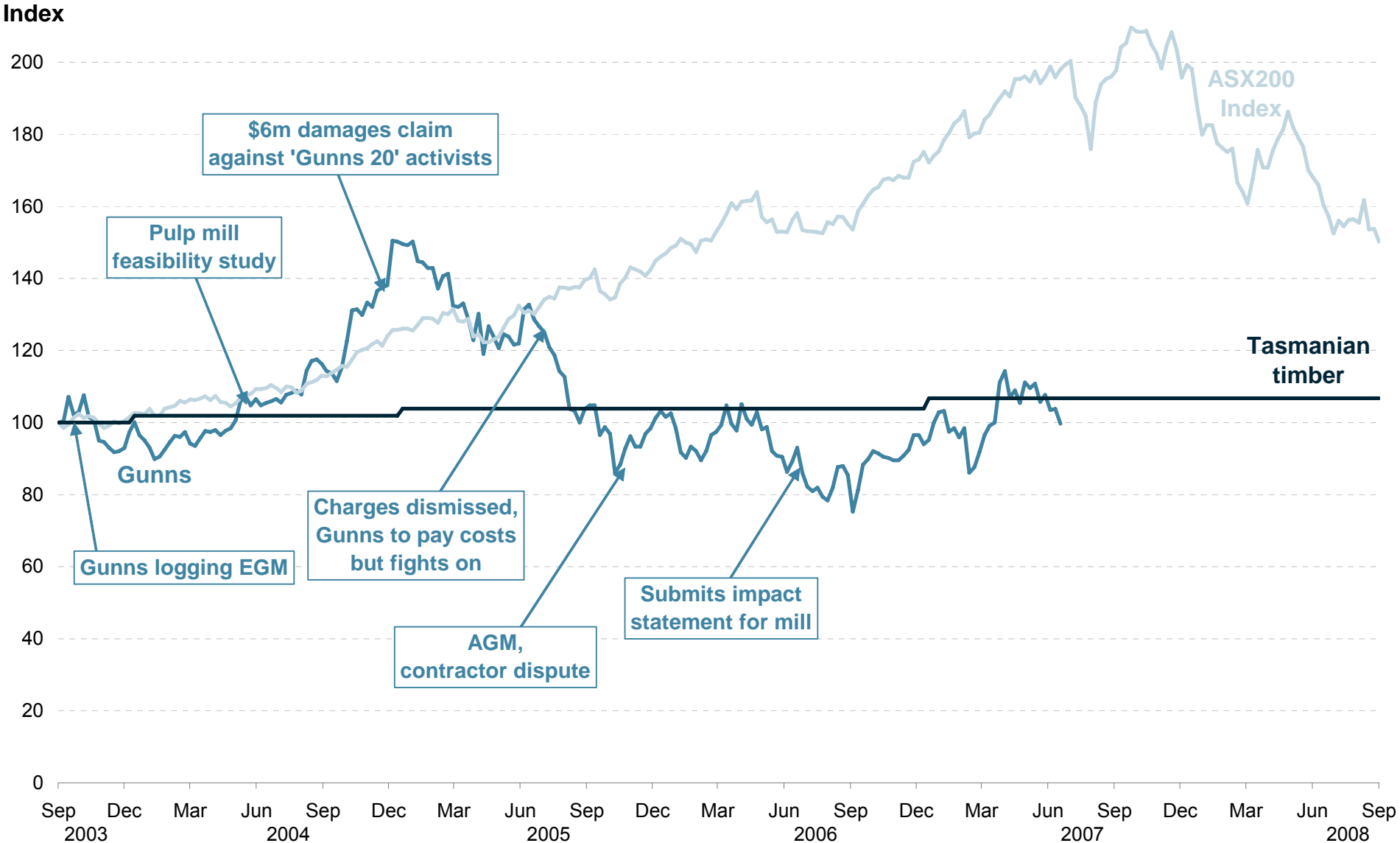
Gunns – 1st case dismissed



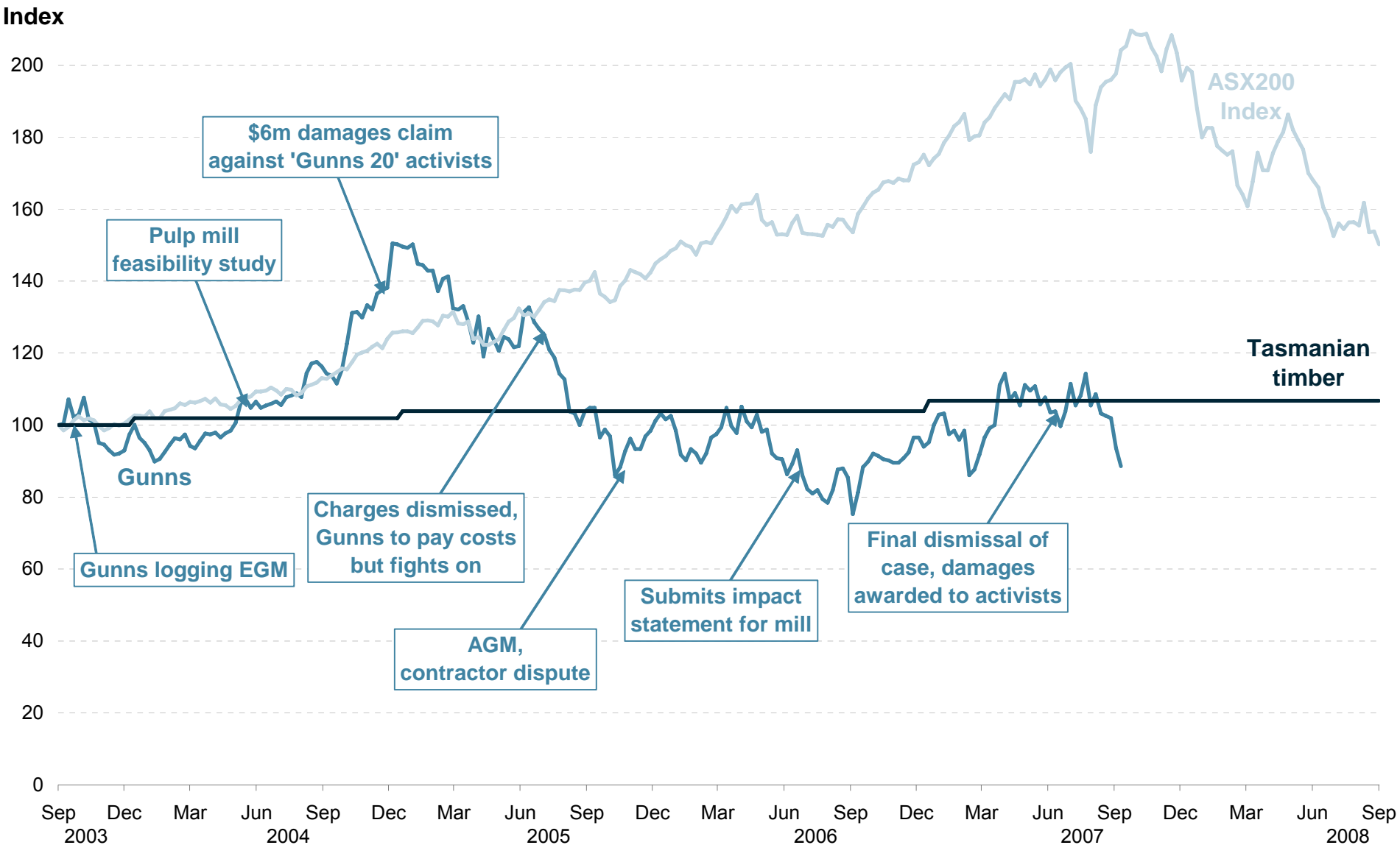
Gunns - Other labor relations issues emerge



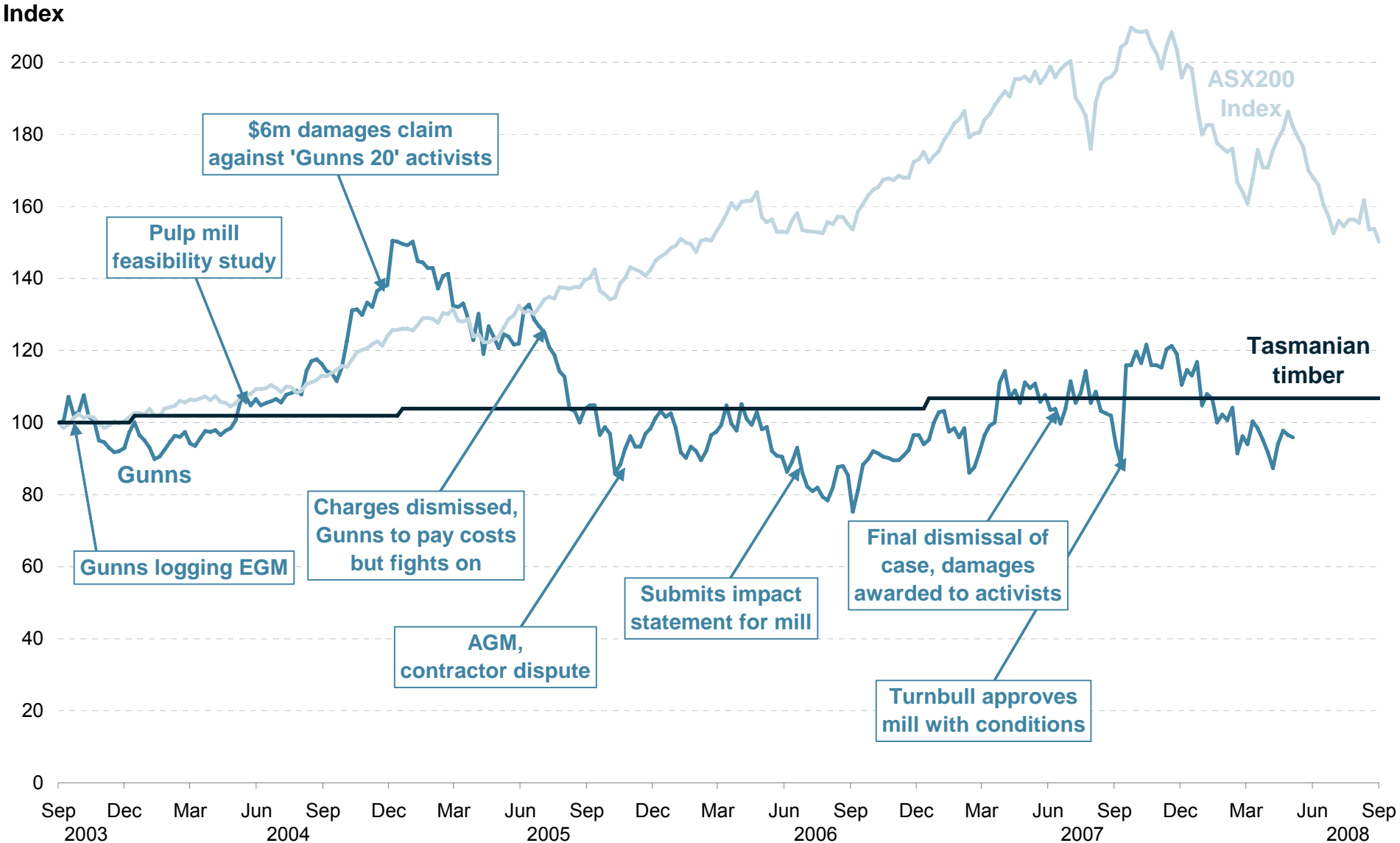
Gunns - environmental credentials put to test



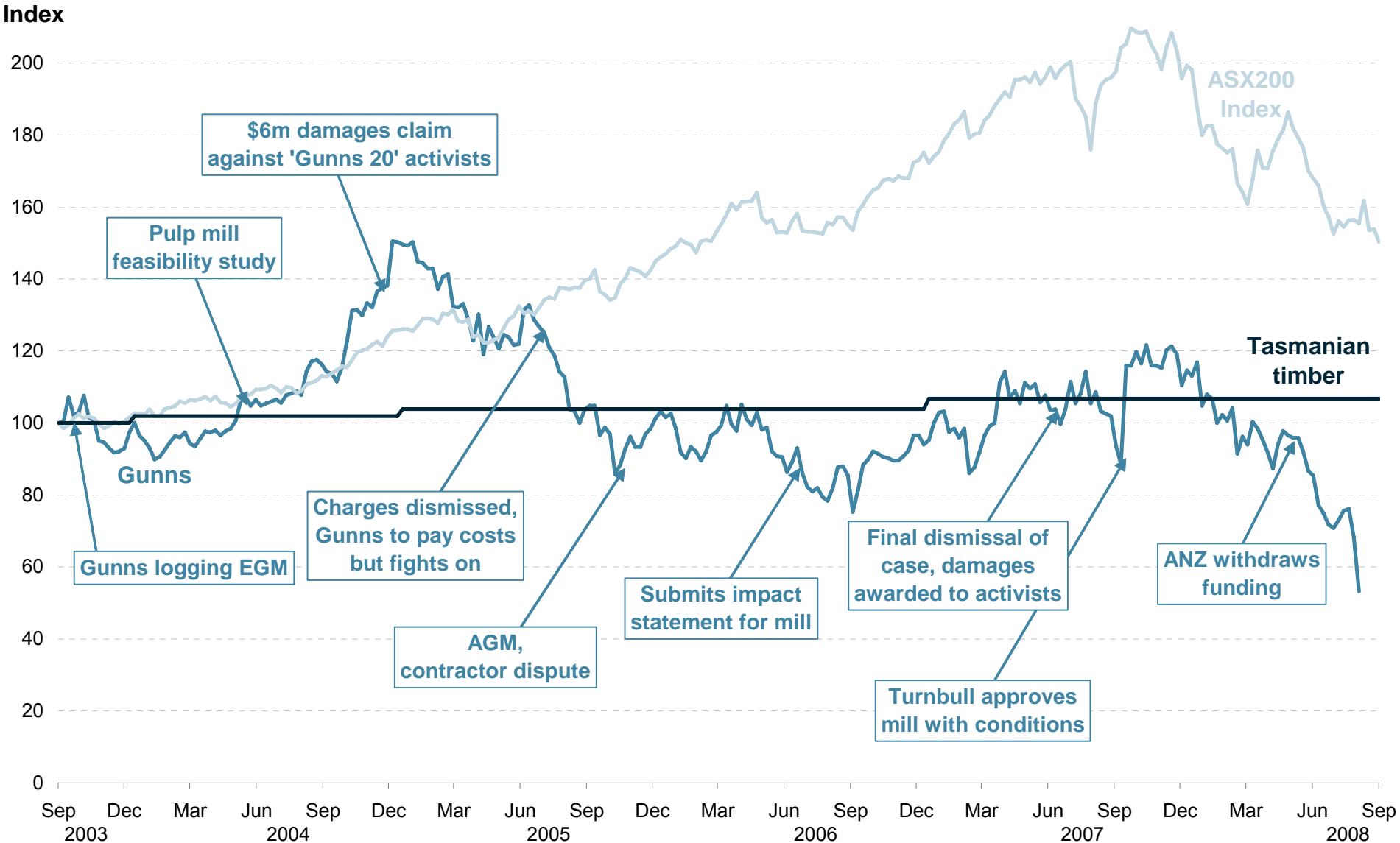
Gunns - Stakeholder and governance headaches **Innovest**



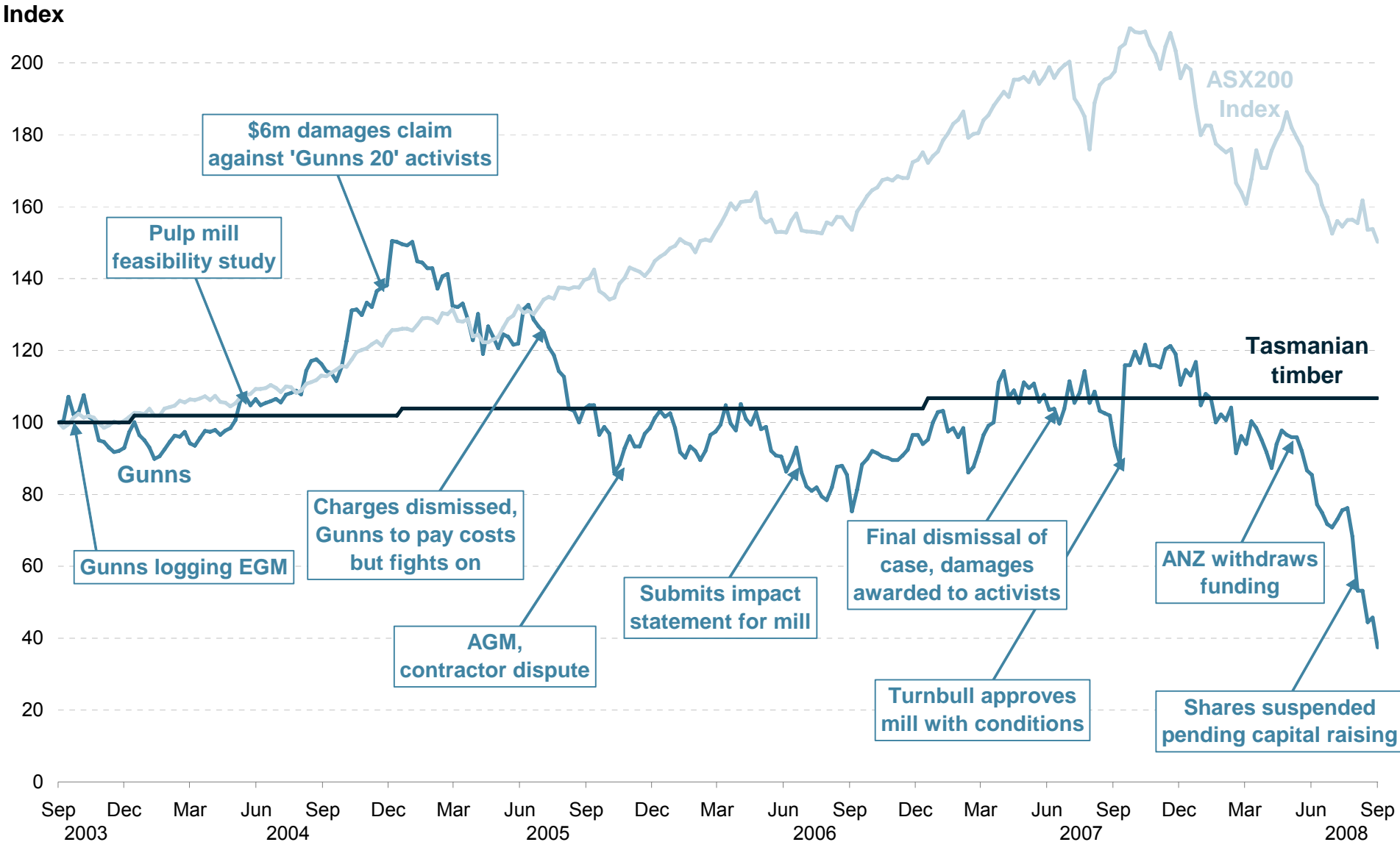
Gunns – Election-driven approval, environmental concerns remain



Gunns - Loses key stakeholder support



Gunns shareholder value pulped – where to from here?



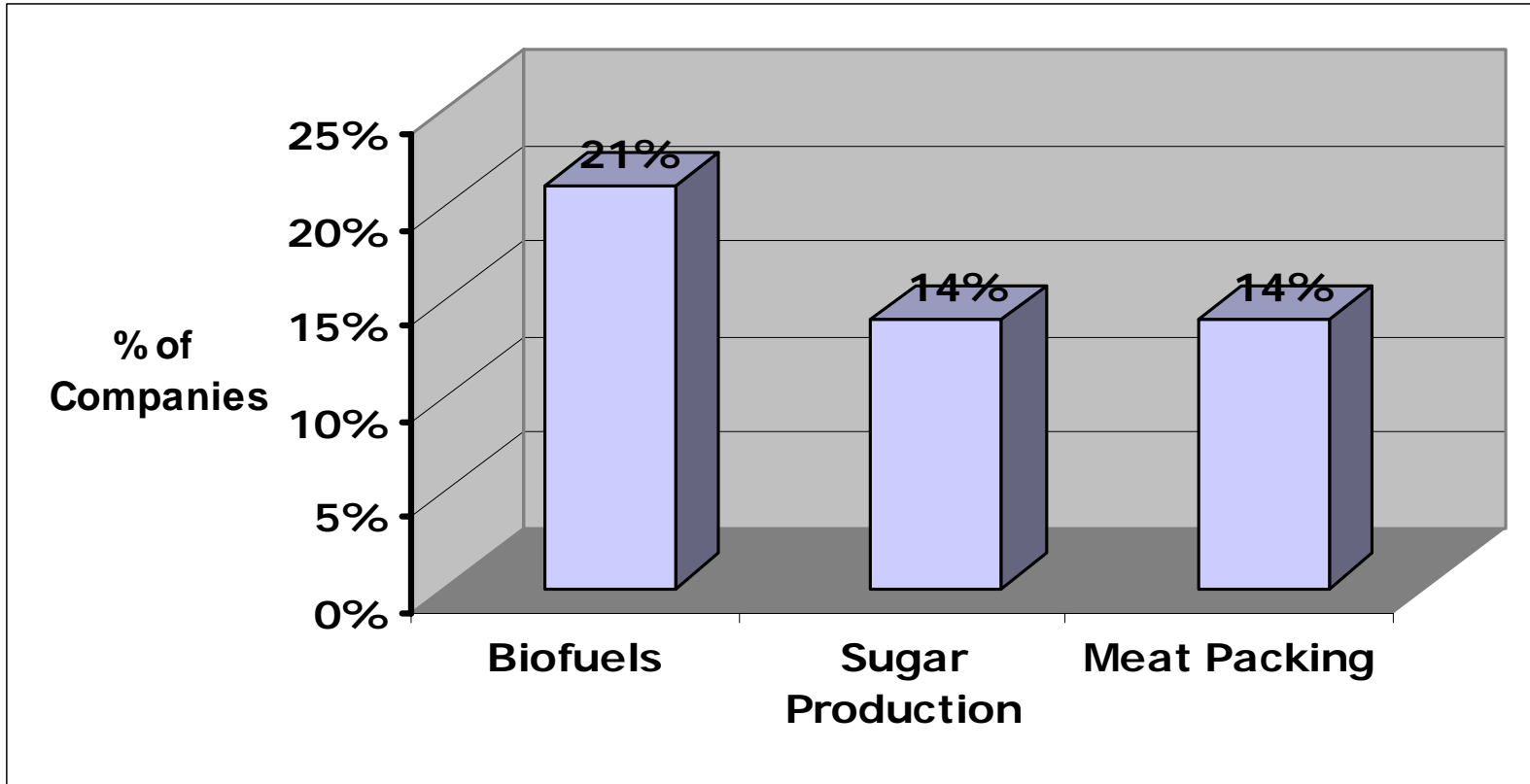
- \$100 invested in 2003 – ASX \$156; Timber \$106; Gunns \$45
- ESG issues are complex, very difficult to manage and represent core business risk
- Environment
 - Ability to gain non controversial key input – timber.
 - Doubts over its commitment to achieve world’s best practice enviro standards for logging operations and the Pulp Mill
- Stakeholder relations
 - Antagonistic approach - unable to gain ‘licence to operate’ status from NGOs
 - Reputation damage amongst community and export clients
- Governance
 - Proximity with Tasmanian govt, long term tenure of Board
 - Inability to understand stakeholders concerns re forests
- ESG issues are not the only factor at play but were significant for Gunns
- Gunns case study highlights the markets short term focus v ESG longer term signal
- Gunns P/E ratio is now 5x – does this represent value for the responsible investor?

Thank you !

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Group Danone (France)

Nestlé (Switzerland)

Unilever PLC (United Kingdom)

Cadbury Schweppes PLC (United Kingdom)

Ioi Corporation Behard - CCC (Malaysia)

Iaws Group – CCC (Ireland)

Tyson Foods Inc – B (United States)

Sara Lee Corp. – B (United States)

Archer Daniels-Midland Company – B (United States)

Leading companies set clear long-term KPI goals and witness annual improvements in areas such as:

Energy Use:

-AAA Company reduced energy use by 12.3% between 2002 and 2006.

Water Use:

-AAA Company reduced water consumption by 20% between 2002 and 2006.

CO2 Emissions:

-AAA Company reduced greenhouse gas emissions 16.5% between 2002 and 2006.

Packaging Material:

-AAA Company reduced packaging waste 315,000 tons between 1991 and 2006.

Hazardous and Non-Hazardous Waste:

-AAA Company reduced total waste levels for disposal by 27% in 2006.

Lost Workdays Due to Accident/Injury:

-AA Company reduced lost days due to accident/injury rate by 40% between 2000 and 2005.

- Innovest Strategic Value Advisors is an international investment research and advisory firm, specializing in analyzing “non-traditional” drivers of risk and shareholder value, and their impact on company competitiveness, profitability and share price performance.
- Rating of more than 2,300 companies globally inc ASX200 and Asian stocks on Environmental, Social and Governance issues with a specialty in climate change
- 55+ analysts, offices in 6 countries on four continents, and clients in over 20 countries. Innovest’s largest outside investor: ABP (Netherlands), second-largest pension fund in the world
- Innovest has been ranked as the #1 global provider of “non-traditional” investment research in both 2007 and 2006 by the Thomson Extel survey of over 140 major institutional investors. Gained several other awards
- In 2007, Innovest is recommended by the Enhanced Analytics Initiative (\$2.6 trillion in combined assets).
- 10 out of the top 25 global asset managers in the world use Innovest research.
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- Innovest clients have collective assets under management of over \$7 trillion
- \$1.3 billion in domestic, international, and emerging markets sub-advisory mandates