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Cocoa value chain analysis

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Value Chain Working Group
Cocoa Value Chain Analysis

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Dutch
Banking Sector
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Executive Summary

The Dutch Banking Sector Agreement (DBA) on International Responsible Business Conduct regarding Human Rights, is an agreement executed among a broad coalition of (Dutch) banks, trade unions, civil society organisations and the Dutch government. The aim of the agreement is to "achieve a material positive impact for people (potentially) facing adverse human rights impacts (related to the activities of clients of the Dutch banking sector) and to search for solutions to address problems that an adhering bank cannot solve by itself."[1] One of the tools developed to that end is value chain mapping. The agreement identifies cocoa as a high-risk commodity that requires further study. This Cocoa Value Chain Analysis identifies areas of potential collaboration to support this commitment in the cocoa sector.

Some 95% of the global cocoa production originates from smallholders, who work on land plots of 1 to 3 hectares. Most of them live in Western Africa, with Ghana and Côte d'Ivoire accounting for 70% of global cocoa production. Many cocoa farmers do not make a living income to provide a sustainable livelihood for their families, let alone invest in their farms and cocoa trees. Low cocoa prices for consecutive years and falling productivity combined with high transaction and high input costs, put pressure on farmers' income and subsequently on cocoa supply. There is no simple solution for the farmers. Switching to other crops is not a feasible option as they lack savings, do not enjoy social protection schemes and do not have access to reliable financing facilities.

In order to preserve their stake in the industry, farmers often obtain loans that have predatory conditions, which further compounds the human rights issues already present. When they default on the financial implications, as they often do, farmers may fall into the debt trap and end up as forced labourers, or some may sell a family member as a slave. Child labour is also commonly present in the cocoa sector. It is estimated that 2.1 million children are working in the cocoa fields of Côte d'Ivoire and Ghana alone.

Dutch banks are relevant players in financing the international cocoa trade. Their main clients are larger trading and processing companies. The DBA-banks feel committed to address human rights issues. At the same time, they are not much

1 Dutch Banking Sector Agreement on international responsible business conduct regarding human rights, available at: *https://www.ser.nl/nl/publicaties/overige/2010-2019/2016/dutch-banking-sector-agreement.aspx*

involved with leading players in manufacturing and retailing, implying that they have limited leverage over companies in this part of the value chain. Further, due to the high-risk profile of financing the production side, banks are hardly involved in financing smallholders as the transaction costs are too high.

Some banks provide advisory services to farmers, local cooperatives, clients and other partners like local banks. Also traders are pre-financing smallholders, but they are limited by liquidity restrictions. Some traders may have supplier codes of conduct which include human rights criteria, but the level of implementation commitment tends to differ significantly. Private and public initiatives like voluntary certification schemes and industry initiatives to increase production and improve its conditions are important, but rather scattered. They have not yet leveraged a multi-stakeholder force for change.

In accordance with the spirit and objectives of the DBA, the parties to the agreement believe there is potential for alignment of initiatives and collaboration between banks, authorities and civil society organisations. Only a solid multi-stakeholder initiative can foster the required positive change in the cocoa sector.

As a result, this Cocoa Value Chain Analysis makes three specific recommendations for concrete action by the DBA and other potential collaborators.

Banks commit to:

- Strengthening existing due diligence practices and mechanisms in the cocoa value chain by sharing best practices and engaging with other banks and relevant stakeholders;
- Building on existing initiatives, improve smallholders' access to finance for cocoa reinvestment, thereby addressing negative human rights impact at farmer families;
- Collaborate with existing sustainability and dialogue mechanisms with the aim to foster a strong multi-stakeholder initiative towards a sustainable cocoa sector with particular reference to the role of and leverage by (Dutch) banks and other financial institutions.

1 Introduction

The Netherlands is the world's largest importer of cocoa and home to the most important cocoa port. It is globally the second-largest cocoa grinder. Dutch banks – both individually and collectively – are important players in financing the international cocoa trade. Against this backdrop, the multi-stakeholder collaboration under the Dutch Banking sector Agreement (DBA) provides a unique opportunity to contribute to addressing human rights issues in the cocoa value chain, to which Dutch banks are connected.

1.1 What is the DBA and why was it initiated?

The Dutch Banking Sector Agreement on International Responsible Business Conduct regarding Human Rights was signed on October 28, 2016 by a broad coalition of (Dutch) banks, trade unions, civil society organisations and the Dutch government. In two ways, its signatories intend to significantly contribute to respecting and protecting human rights by banks:

1. By further implementing the responsibility to respect and protect human rights in banks' operations and relationships; and
2. Via collective action by banks and stakeholders, addressing challenges that an individual bank in certain value chains cannot solve on its own.

The DBA identifies a number of areas where banks and other parties are taking action and collaborating, including human rights due diligence and reporting, as well as on developing and implementing tools that banks and other parties can use to support the commitments made. Carrying out joint value chain mappings is one of the key exercises agreed upon in the DBA.

1.2 What are the objectives of the Value Chain Working Group?

DBA's Value Chain Working Group maps high-risk sectors that are material to Dutch banks, starting with the cocoa, palm oil and gold value chains. Working group members include representatives from banks, the government and civil society.

These value chain mapping exercises contribute to developing shared knowledge and resources by pooling data and expertise. They also facilitate knowledge exchange on how banks – both individually and collectively – can exercise leverage in high-risk value chains.

Because Dutch banks finance companies that are active in the cocoa value chain, we have a responsibility to address adverse human rights impacts, such as child labour. Our multistakeholder collaboration enables us to better understand the root causes of those impacts, evaluate existing initiatives and explore what we can do more or differently in order to contribute to a more sustainable cocoa value chain.
Ruben Zandvliet, ABN AMRO, member of the DBA Value Chain Working Group

The DBA Steering Committee, comprising all parties in the agreement, will draw conclusions from the results of the value chain mapping exercises, and advise adhering banks on follow-up activities.

1.3 What are the objectives of the cocoa value chain mapping?

The primary goal of the cocoa value chain mapping, is to make a substantial contribution to reducing adverse human rights impacts in the cocoa value chain. In order to do so credibly and effectively, the DBA Value Chain Working Group broke this goal down into four key objectives:

Objectives Cocoa Value Chain Analysis			
I. Understand the **nature of adverse human rights impacts** and the connections with Dutch banks' activities and business relationships;	II. Understand the **root causes** of adverse impacts and which approaches have the best potential for making a positive **change** in the cocoa value chain;	III. How Dutch banks and other parties can best **contribute** to these approaches and to positive change;	IV. The **barriers** to implement and identify **creative and constructive ideas for action** in the cocoa value chain.

1.4 What is the methodology?

The DBA applies the OECD Guidelines for Multinational Enterprises (OECD Guidelines) and the United Nations Guiding Principles on Business and Human Rights (UN Guiding Principles) as its normative framework. The working group, supported by Shift,[1] developed a methodology for its analysis building on the described framework. It also used experience gained from a workshop on the

1 Shift is a leading center of expertise on the UN Guiding Principles on Business and Human Rights and has been supporting the Ministry of Foreign Affairs and the SER in various ways in facilitating the Dutch covenant process.

identification and prioritisation of human rights impacts, organized by SER and facilitated by Shift in 2014.[2] The full methodology is provided in Annex 1. Through desk research, interviews with banks' staff, presentations by experts and discussions with members of the working group, the lead bank for this value chain mapping (ABN AMRO) developed an initial analysis of the key objectives. This was shared with a broad group of stakeholders and experts for comment and feedback. This group then carefully examined the main question of the analysis: how banks and other parties can best contribute to reducing adverse human rights impacts in the cocoa value chain. The working group then further developed, refined, and agreed upon the main recommendations as a result of our findings, as laid out in this paper.

1.5 What is the scope of this paper?

The scope of this paper is delimited in three ways. Firstly, as the focus of the DBA is on the banks' responsibility to respect and protect human rights, other impacts such as climate change and other environmental issues have been taken into account only in so far as they are material to the root cause of adverse human rights impacts in the cocoa value chain.

Secondly, concerning the geographical scope, the value chain working group focuses primarily on Western Africa, where the major cocoa producing countries are. Severe human rights impacts are reported from this region, which implies that the potential positive impact (i.e., number of people affected) is high.[3]

Thirdly, this paper reflects on the role of the *Dutch* banking sector in the cocoa value chain; the analysis of the (root causes of) human rights impacts is therefore not exhaustive.

> *This is not the first paper about the cocoa chain and will not be the last. Yet, what makes this paper distinct and worth reading, is the role of the financial sector in cocoa chain development; what can (Dutch) banks do to further enhance sustainability and reduce human rights violations in the cocoa value chain. For, don't we all want our chocolate bar without bad aftertaste? Now, this requires collaborative action. Chain stakeholders need*

2 Reference report *https://www.ser.nl/~/media/files/internet/publicaties/overige/2010_2019/2014/themarapportage-due-diligence-shift-ser-workshop.ashx*

3 This is not to say that in other countries cocoa cannot be involved with human rights impacts – indeed during the analysis it was pointed out that cocoa production can be connected with various human rights impacts that may not occur in Western Africa.

to join hands. The multi-stakeholder collaboration under the Dutch Banking Agreement is a firm step forward. Not the first step and not be the last. Yet, a sustainable step worth following towards sustainable cocoa!"
Rogier Verschoor, Oxfam Novib, member of the DBA Value Chain Working Group

1.6 Structure of this paper

This paper is structured into four parts. In chapter 2, the cocoa value chain is briefly analysed and an assessment is made on the role of Dutch banks in financing the cocoa trade. In chapter 3, notorious human rights impacts in the cocoa value chain are described and their root causes identified. In Chapter 4, predominant current (sectorial and company specific) approaches to address these human rights concerns are considered. Based on this analysis, the document closes in chapter 5 with a set of three concrete recommendations for follow-up action by the Dutch Banking Agreement working group and potential collaborators.

2 Mapping the cocoa value chain

2.1 Why are we mapping the value chain?

Human rights impacts occur in a variety of ways across the globe on a daily basis. Banks have obligations under the UN Guiding Principles (among others) and the manner in which this is fulfilled depends on their role in their financing relationships with clients. Evaluating their impact requires a nuanced approach in order to have the best information and perspective available. One of the tools that is considered beneficial to this end is value chain mapping. This allows banks to pinpoint where the impact of its involvement can be found and how they can apply leverage to mitigate or address human rights impacts. Specifically, value chain mapping helps to:

- Clarify responsibility: Which responsibilities should banks take into account, according to the UN Guiding Principles and the OECD Guidelines?
- Prioritise efforts: Where do the most severe human rights impacts occur and, subsequently, on what should banks, with the support of other parties, first focus their efforts?
- Understand Leverage: How exactly are banks connected to human rights impacts and where can they create most leverage in the value chain to effectively prevent, mitigate and remediate these impacts?
- Analyse solutions: What are the root causes and challenges in a particular value chain and how best can they be addressed, including identifying who needs to be involved?

2.2 Who are the key actors and what are their finance needs?

Cocoa is one of the world's most savoured agricultural products, mainly in the form of chocolate. It is grown by smallholders who produce 95% of all cocoa, usually on plots between 1-3 hectares. Many of these smallholders live in West Africa, which accounts for 70% of the world's cocoa production. Millions of farmers depend on cocoa to make a living. Still, they face many challenges, making it impossible for them to earn a decent income to provide for themselves and their families. For example unproductive fields or low farm gate prices. Since September 2016, the price of cocoa per tonne has fallen from an average of $3000 to $2000. Smallholder cocoa farmers have seen a sharp decline in their income from cocoa (by far their most important income source). Farmers cannot switch easily to other crops, given the long life-span of cocoa trees and the fact that farmers do not have any savings, social protection schemes or access to credit/finance. At the same time, child labour remains commonly present in the cocoa sector. It is estimated that 2.1 million children are working in cocoa fields in Ivory Coast and Ghana alone. The picture below indicates the various steps that make up the cocoa value chain. The box below further describes the cultivation, processing, manufacturing and consumption of chocolate.

Chocolate: from farming to consumption

Cocoa farming

Cultivation. Cocoa can be grown within 20 degrees north and south of the equator. Cocoa trees are sensitive andrelatively vulnerable to disease, climatic conditions, and fertilisation in order to reach commercially attractive yields. Cocoa trees are most productive between 5 and 15 years of age. The market distinguishes between 'fine' or 'high flavour' (criollo) beans and 'ordinary' or 'bulk' beans (forastero). The first category is grown in Latin American and the Caribbean and is used for fine chocolate and bars of high cocoa content. The latter category of bulk beans is predominantly grown in Western Africa and accounts for a far larger market share. It is used for chocolate products at the lower end of the market, with low cocoa content and a high percentage of sugar.

Harvest. Cocoa can be harvested several months a year, but the peak cocoa harvest is twice a year. When exactly, varies from country to country. The production during these two periods is known as mid-crop and main crop. Forastero mid-crop beans are smaller and of inferior quality. They are normally used and processed locally, while the better quality main crop beans are exported.

Removing the beans. After harvesting, the cocoa pods are opened to remove the beans. In Western Africa they are then fermented on heaps or piles covered by banana leaves, while in Latin America the fermenting is mostly done under controlled conditions in large boxes. The beans must be stirred each two to five days. Fermentation causes the beans to develop flavour and colour. This is a natural chemical reaction, which takes between five to eight days depending on the climatic conditions. Subsequently the beans are dried, either out in the open (in the sun) or in a gas- or sun-heated drier. The dry cocoa beans are packed and ready to be sold.

Preparing beans for export

Many farmers in African countries sell their beans to local buying stations or agents, which in turn supply the international cocoa traders. These traders typically have large warehouses in coastal areas where the quality of the beans is checked and batches are prepared for shipment. Other organised farmer groups, associations or cooperatives sell their beans collectively to leverage negotiating power vis-à-vis traders. Sometimes collectives directly sell to exporters.

Processing of cocoa beans

After shipping, the beans are stored in traders' warehouses in the importing countries. From there, they are transported locally to processing facilities. Deliveries take place on a 'just-in-time' basis, meaning that the processing facilities themselves keep stock of minimal quantities of beans.
At the processing facility, the cocoa beans undergo their main transformation. After they are roasted, the nib (the inside of the cocoa bean) is ground into paste. The heat creates cocoa liquor, which can be further refined into cocoa butter, cocoa cakes (or pulverized into powder) and cocoa mass (solid cocoa liquor), which are sold to chocolate manufacturers.

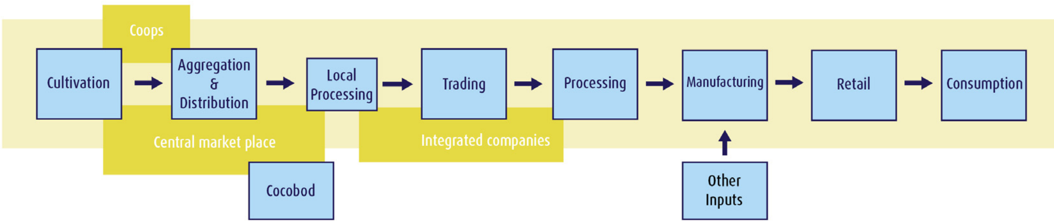
From bean to end-product

There are many different end-uses of cocoa liquor, powder and butter. At this stage, the cocoa value chain interacts with other agri-commodities' value chains, such as sugars and nuts. Demand for chocolate and cocoa butter is also increasing in the pharmaceutical and cosmetic industries.

Retail

Chocolate is sold in countless shops all over the world. Even the largest retail companies only account for a small portion of global sales. While organic stores may only sell organically certified chocolate, the majority of shops will sell both certified and conventional chocolate, leaving the choice to the consumer. This assumes that such a choice exists, but consumers are often unable to make an informed decision whether or not the chocolate cake they buy, contains responsibly sourced cocoa. In general, consumer demand for certified cocoa is growing, but is still smaller than the global supply of certified cocoa. Different labels are popular in different consumer markets. For example, as far as social compliance labels are concerned, the Dutch chocolate market is clearly dominated by Rainforest Alliance / UTZ Certified.

Figure 2.1 Key Actors in the Cocoa Value Chain



The following aspects and developments are particularly relevant to this value chain analysis:

- Each link in the chain comprises a large variety of entities: from millions of smallholder farmers in production, to a handful of dominating international traders and manufacturers;
- Governments, particularly in Ivory Coast and Ghana, are central players in the value chain: the Government of Ghana requires that all beans are sold through its central marketplace (Ghana Cocoa Board, Cocobod) and regulates prices for producers and buyers; in Ivory Coast the Conseil du Café-Cacao (CCC – the marketing board managed by the state) is responsible for price stabilisation systems, based on the forward sale of cocoa.
- There is a strong development of vertical and horizontal integration in processing and trading: there have been many takeovers and mergers in the past few years, creating very large players in these parts of the value chain.

The following table further illustrates several of these aspects.

Step	Type of entities	Type of financing
Cultivation	Millions of smallholder farmers.	This part of the value chain is financed to a large extent by local banks and cooperatives, as well as in informal ways by traders, input suppliers, middlemen or moneylenders. There is an enormous gap between the demand and supply for smallholder finance. Cocoa cultivation may not require much working capital; reviving cocoa farms will require a lot of investment capital over the years to come; Annual interest rates are often excessive.
Producer organisations	Thousands of farmer organisations. Level of organisation differs. Majority of cocoa farmers is not organized.	
Aggregation & distribution	Itinerant buyers, local traders and middlemen buy up cocoa from smallholder farmers who are not organized in cooperatives.	

Step	Type of entities	Type of financing
Central market place	State agents like the Ghana Cocoa Board (Cocobod) and the Ivory Coast government Conseil du Café Cacao (CCC).	Cocobod is financed by international banks through syndicated loans, including hedging facilities*.
First processing (cocoa mass, butter and powder)	Facilities owned by the large integrated traders as well as local companies.	Some financing by international banks through bilateral or syndicated loans.
Trading Processing into chocolate couverture	Market dominated by five players: Cargill, ECOM, Olam, Barry Callebaut, and Touton.	Some traders are listed on a stock exchange through which they raise equity. All trade companies are financed by international banks through bilateral or syndicated trade commodity finance, as well as through corporate bonds.
Manufacturing into bars, chocolate and other end products	Thousands, with a few dominant players like Mars, Ferrero, Mondelēz, Meiji and Nestlé.	Some manufacturers are listed on a stock exchange. All large companies are financed by international banks through bilateral or syndicated credit facilities, as well as through corporate bonds.
Retail	Includes everything from large supermarket chains to the local chocolate shop around the corner.	Larger players are also financed by international banks through bilateral or syndicated loans, smaller players have bilateral relationships with local banks.
Consumption	Billions of consumers.	Not applicable.

* During the interviews for this analysis, it was mentioned that the Ghana Cocoa Board (Cocobod) has a syndicated loan facility (including a hedging facility against fluctuating market prices), and that several Dutch banks are part of this syndicate.

2.3 How are banks connected to this value chain?

The Bulk: Trade Commodity Finance

Dutch banks are mainly involved in the cocoa value chain via trade commodity finance activities. They facilitate the financing of shipments of bulk cocoa beans from producing countries to processing facilities. There are roughly three options for financing trading clients: transaction based, borrowing based and balance sheet.

3 Options for Trade Commodity Finance	
Transaction based	When a bank finances a particular stock of cocoa beans that one of its clients is buying (to be sold later to processors and onwards to manufacturers), it may issue a credit line based on a document that verifies that its client actually has control over the particular stock of cocoa (so called bill of lading). The banks could also have a pledge over the goods. This is to assure the bank that in case of default, it becomes a senior creditor over the stock and would be able to recuperate the credit it issued by selling it to another party.
Borrowing based	This option entails issuing loans are not tied to specific trade flows, but may be used for general purposes. The balance of assets and liabilities of the client (the borrowing base) determines the maximum size of such credit facility. Credit is extended based on weekly/ monthly assessments of the client's borrowing base. Most of the time, the collaterals are made of inventories, receivables and cash received from end-buyers.
Balance sheet	This is typically for the larger trading (and processing) companies, which have multiple sources of long-term finance. Balance sheet financing essentially means that the client has sufficient assets convincing the bank that it is unlikely that the client would not be able to repay its loan. Often these loans are "syndicated," which means that multiple banks jointly provide the loan, because the credit need of the client is too large to cover for one individual bank. Such syndicates enable multiple banks to share possible risks.

The choice between these three types of financial services depends on the risk-profile and size of the client. New relationships typically start with transaction-based financing. Large trading companies are normally financed through balance sheet financing. Because of the general purpose of this type of loans, banks do not necessarily request what they are used for. It may be for trading of cocoa or for another commodity, or it may be for processing or some other activity.

To some banks, balance sheet financing for clients that are (also) involved in cocoa trading may be part of trade commodity finance, while for others it is part of a different business unit or department, namely corporate lending (could also be named wholesale banking or corporate finance). Overall, the types of activities and products offered among the three major Dutch Banks (ABN AMRO, ING and Rabobank) are very similar.

Limited to no involvement before processing

The involvement of Dutch banks in directly financing smallholders or producer organisations (like cooperatives) is very limited. This is partly because they have limited presence in producing countries, but the main reason is the relatively high transaction costs to finance the production side. The regulatory systems of Dutch banks often consider loans to local banks or producer organisations as too risky. Moreover, many banks consider transaction costs to be too high for a competitive rate while completing their formalised processes.

However, some banks have been exploring impact banking initiatives (with others following suit); these are targeted at smallholders in different agri-commodities, including cocoa.[1] Financing of smallholders typically involves a third party, which could be a client that is also part of the cocoa value chain, or a financial institution with local operations.[2]

In addition to financing smallholders, some banks provide advisory services to farmers, local cooperatives, clients and other partners, including local banks. Examples include:

- Rabo International Advisory Services, a part of Rabobank, helps in establishing and professionalising cooperatives, for example by introducing mobile banking services.
- The ABN AMRO Social Impact Fund participates in a social enterprise, SCOPEinsight, that focusses on improving the entrepreneurial skills of smallholder farmers, such as SHFs in cocoa cooperatives in Ivory Coast.
- FMO is working with trading company Ecom to develop and test Key Performance Indicators that measure impact on smallholder livelihood.

Financing manufacturers and retailers

Involvement of Dutch banks with the top-10 players in manufacturing and retailing is limited, meaning that Dutch banks have limited commercial leverage in this part of the value chain. One Dutch bank maintains a relationship with a chocolate manufacturer which is a registered social enterprise. Retailers are diverse and widespread and there is significant servicing by banks of these clients. However, banks will not finance specific cocoa activities of these clients, because there is no such demand. Retailers that focus on chocolate products specifically, are typically very small.

In this part of the value chain, the connections between banking activities and the actors in the chain are less specific than for instance in trading. However, this value chain analysis highlights that both manufacturers and retailers can (and should) play an important role in driving change in the value chain, because they are consumer facing and likely more sensitive to public pressure. Indeed, the major chocolate producing companies all have cocoa sustainability programs and some retailers play an important role in raising consumer awareness.

1 See for example ING (https://www.ing.com/ING-in-Society/Sustainability/Societys-transition/Impact-finance.htm) and ABN AMRO (https://www.abnamro.com/en/newsroom/blogs/liesbeth-kamphuis/2017/impact-banking-access-to-finance-helps-farmers-escape-poverty.html)

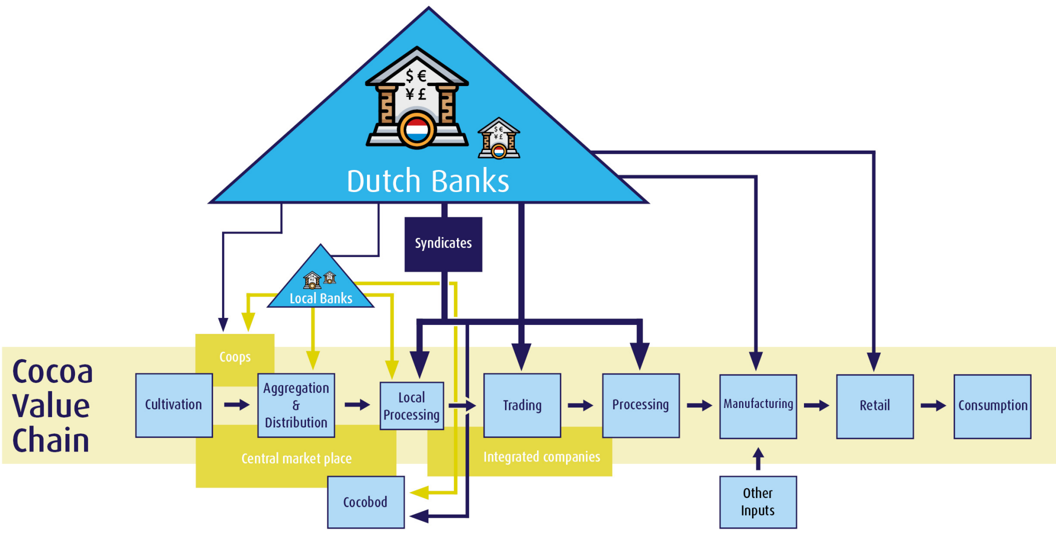
2 <geen tekst in het Word document, laten vervallen?>

3 Human rights impact in cocoa

3.1 Human rights impact in the cocoa value chain

The UN Guiding Principles require national States to protect human rights, while businesses have a responsibility to respect and protect human rights in their own operations and throughout their value chains. Compliance to these UN Guiding Principles also requires an appropriate remedy system to be in place when human rights are violated. The main human rights impact in the cocoa value chain was discussed extensively in the working group and described in this analysis. The working group recognises that this overview is concise and non-exhaustive.

Figure 3.1 Connection of Dutch Banks to the cocoa value chain



The right to an adequate standard of living

Each person has the right to provide for adequate food, clothing, housing, medical care and other basic needs of his/her family. In the cocoa sector, this is translated into the right of farmers to obtain a living income from growing and selling cocoa pods and beans. As most of the small-scale cocoa farmers dedicate part of their time and other resources to alternate crops, this is being accounted for when calculating the living income from cocoa. This right also applies to cocoa farm and plantation labourers, as well as to factory workers who need to make a living wage to reach an adequate standard of living for them and their families.

For several years in a row, farm gate prices in the main cocoa producing countries have supported neither a living income to smallholder farmers, nor a living wage to farm labourers. Many cocoa farmers had no other option than to postpone (or cancel) reinvestments in their cocoa trees and farmlands or other productive inputs. Their crop revenues and family income turned out to be insufficient to support these investments. In fact, over the past years numerous cocoa farmers in West-African got trapped in a vicious circle of deprivation. Low farm gate prices for years, in combination with poor access to (natural, social, financial, human and physical) capital required to break this circle, have worsened the living standard of countless families dependent on cocoa production for their livelihoods.

Child labour

Children as young as six years old are engaged in child labour in smallholder and family cocoa production in countries like Ghana and Ivory Coast. A report by Tulane University in 2015 revealed that during the 2013-2014 cocoa harvest season approximately 1.2 million children between the ages of 5 and 17 had been employed in the cocoa sector. Children participate in many cultivation and harvest activities, including collecting and opening cocoa pods, drying the beans and transporting them to local trading points.

International treaties do not allow for child labour, and legislation in both Ghana and Ivory Coast restrict the type of work children under 15 and 14 are allowed to do, given its hazardous nature. Nonetheless, children are exposed to extensive working hours, and sustain multiple injuries due to the use of sharp tools and unprotected use of pesticides, and overstraining children's bodies due to excessive weight carrying.

> *For decades we have been trying to break the cycle of child labour. Unfortunately, we have not yet been able to do so. Through the years we've learned that child labour is interlinked with a wide variety of issues and has multiple root causes. To eliminate child labour, these issues have to be addressed simultaneously, involving all stakeholders. This includes involving and speaking with children, since it directly affects their lives. Only then can the cycle be replaced by a new sustainable system in which children can develop and have a bright future.*
> Jaap Bartels, Save the Children, member of the DBA Value Chain Working Group

Migration for agricultural work during peak season is common practice in Ivory Coast and Ghana. Children both migrate with and without their families for work, posing serious protection issues like, for example, the risk of exploitation, physical and psychological harm. These risks tend to be higher to girls than to boys. Furthermore, children are trafficked into working on cocoa farms, depriving them from their liberty and rights. Quantifying the number of children that are trafficked is challenging due to its hidden nature.

Forced labour

In the cocoa sector the prevalence of modern slavery and forced labour practices are high. The causes for these severe human rights violations are linked to the rural poverty or deprivation trap in numerous agri-based sectors and countries in Western Africa. Farmers often fall victim to predatory loans, which causes them to go into debt. They may take on loans at even more demanding (or even impossible) conditions. After a while, such farmers may be in such despair that they sell a family member as a slave, or become a forced labourer themselves. Usually the moneylenders are informal and powerful people in their localities or regions.

Countries like Ghana and Ivory Coast host large groups of people from neighbouring countries like Burkina Faso and Mali, who migrate during the dry season in search for water and work. These people are vulnerable to exploitation and they are often found in forced labour positions on cocoa farms. Incidents have been reported of foreign workers spending their nights in the forest and being transported by 'employers' to work long days on cocoa farms and plantations for seven days a week with their entire families. Unfortunately, such modern slavery is an every-day-reality in the cocoa sector.

Land rights

Many farmers have no official land titles, as they often have received the right to use the land via informal or traditional tenure systems. The lack of tenure security is one of the main reasons for poor productivity of cocoa farms, as farmers are not inclined to invest in the land or take care of their soil and trees properly. Cocoa farms are often un-mapped and farmers lack proper land documentation. Tenant farmers lack formal written contractual arrangements and are hesitant to replant old or diseased cocoa trees out of fear that they would lose the access to their land if they would cut down trees on it. Land titles are often required as collateral for formal loans. As such, many farmers cannot access formal financial services and thus turn to informal moneylenders or traders for loans.

3.2 What are some of the causes of these human rights impacts?

The DBA and its value chain analysis want to substantially contribute to reducing human rights impact in the cocoa value chain. It is therefore important to understand how the above mentioned human rights impact is interrelated and what root causes are. Without such root cause analysis, any proposed solution or action may be ineffective or temporary. Some of the most raised explanations are given in this paragraph.

Weak governance and institutions

The political context of many countries in which cocoa is grown, is a primary source of human rights risks. When looking at Ghana and Ivory Coast, weak governance structures affect cocoa farmers. Lack of registration and protection of property hinders investments. In Ghana, about 70% of all court cases are about land titles.[1] When a farmer has no proper legal documentation on the ownership of a plot, he/she will not replant unproductive trees. The low availability and quality of education in rural areas creates high levels of illiteracy. This limits the ability of farmers to educate themselves, or be educated, about good agricultural practices as well as the prospects for establishing professional cooperatives. Illiteracy and low education levels may also have significant health and safety risks, as farmers are not handling pesticides and fertilizers as intended. In addition, children and youngsters are hindered in their education and personal development to help themselves and their families to escape out of poverty.

Lack of bargaining power by cacao smallholders

Over the last years, large trading companies have integrated both horizontally and vertically. Horizontal integration means that trading companies merge and become larger. Vertical integration reflects that traders also become processors, both in producing countries and in destination countries (i.e., where manufacturers are based) and third countries (like the Netherlands and Germany, which are major trading and processing hubs). On the other hand, many cocoa farmers are not well organised. Combined with market concentration, this could create an asymmetry within the cocoa chain and might further weaken the bargaining power of farmers.

1 Ehwi, Richmond J., Lewis A. Asante (2016) *Ex-Post Analysis of Land Title Registration in Ghana Since 2008 Merger Accra Lands Commission in Perspective.*

Lack of finance for reinvestment

In addition to a general lack of access to financial services for farmers and cooperatives, there is a vast shortage of capital that enables long-term investments. Many cocoa trees are old and unproductive and should be replanted. But many farmers do not invest, as this would reduce their income for some 4 to 5 years, while the farmland may not even be theirs and the access to investment capital is tough.

Gender inequality

The role of women in cocoa production is usually undervalued. It is estimated that about 25% of the farms in Ghana are owned by women. Furthermore, women tend to have designated tasks in cocoa production, also when farms are owned by their husbands, sons or other male family members. Though they play a large role in production, they are usually unpaid (family labour) and do not receive much support or training.

In main producing countries, the producer organisations like cooperatives or associations have relatively high barriers of entry for women farmers. This reinforces the male domination in the agricultural sector as a whole, and in a cash crop like cocoa in particular. Female farmers also suffer from discrimination and encounter structural bottlenecks to gain access to loans and other financial services from rural banks, cooperatives and formal finance providers.

4 Current human rights approaches

4.1 What types of due diligence are exercised by players in the value chain?

Traders

Different actors in the cocoa value chain have different drivers for human rights due diligence. In the past, traders faced legal claims concerning child labour.[1] Their primary concern is to guarantee product quality and ensure long-term supply. They intend to achieve this by developing a class of professional cocoa farmers, who are better trained and financed than the current average farmer.

Financing of smallholders does not necessarily mean that they receive credit. Often, traders supply inputs (seeds, fertilizer and agro-chemicals). This supports farmers in their annual production cycles, but this does not allow for long-term investments in diversification of their farm or replanting of cocoa trees. Experts warn that these types of trade finance, which include off-take agreements, create a dependency that may ultimately hurt farmers. Market entry by other financial service providers (including new ones like mobile money providers) could drive down interest rates or improve farmers' access to tailor-made services such as investment lines for replanting or farm upgrading.

In addition to programs aimed at increasing productivity, traders have supplier codes of conduct which include human rights criteria. When they have clients that produce certified cocoa products, the traders are part of the chain of custody for certified cocoa as well. Whether traders' policies and approaches are fully aligned with the UN Guiding Principles, OECD Guidelines and the Children's Rights and Business Principles, has not been systematically assessed. The level of information on how traders put their commitments into practice differs significantly. More transparency is required to assess if due diligence is indeed effective.

Manufacturers

Traders are actors in the value chain that are relatively unknown to the general public. Companies like Mars, Nestlé and Ferrero however, are well-known and have consumer brand names to protect. Their 'vulnerability' to reputational damage is

1 See: https://business-humanrights.org/en/nestl%C3%A9-cargill-archer-daniels-midland-lawsuit-re-c%C3%B4te-divoire

demonstrated by high profile court cases and allegations of trafficking, slavery and inhumane treatment on plantations. While no company has been convicted, there is much pressure on manufacturers to demonstrate responsible sourcing practices. Mars, Nestlé and Ferrero have therefore strongly committed themselves to source 100% certified products by 2020.

Barry Callebaut

Barry Callebaut has a commitment to eradicate child labour in its supply chain by 2025. It has piloted a CLMRS together with the International Cocoa Initiative. The CLMRS has facilitators on the ground who work in communities to track and remediate cases of child labour, and pinpoint contributing factors. The company has KPI's on the number of child labour cases that are identified and remediated, and on the percentage of farmer groups and suppliers that have CLMRS systems in place.

Nestlé

Nestlé is one of the largest chocolate manufacturers in the world. Through its Nestlé Cocoa Plan the company aims to improve agricultural practices in cocoa producing countries. Like Barry Callebaut, Nestlé has established a Child Labour Monitoring and Remediation System (CLMRS) and published a dedicated Child Labour Report in 2017. The CLMRS is integrated with Nestlé's supply chain in Ivory Coast and is in the early stages of adoption in Ghana. Because there is no 100% traceability back to the farm, Nestlé is working with farmers and cooperatives whose supply may (also) end up in the end-products of their competitors. Its 2017 Report states that child labour in the company's supply chain has been reduced by 51% in a three-year period.

Like traders, manufacturers are working with local communities. Nestlé for example, reports that it will increase the coverage of the 'Nestlé Cocoa Plan' from 33% to 57% of its total supply. More involvement in the upstream part of the supply chain by manufacturers means that they become more interesting partners for banks in smallholder financing projects, as banks typically work with third parties that have direct connections with farmers. The part of the upstream supply chain in which manufacturers have no direct involvement is covered by supplier codes of conduct, but it is difficult to create transparency in this respect. Also, there is no unique standard nor reference for manufacturers' codes and schemes yet. The new

ISO/CEN 34101 standard (yet to be approved and introduced) is expected to provide more analogy and opportunities for benchmarking, which will make it easier for banks to engage with their clients on this subject.

Retailers

Banks have (tens of) thousands of clients, meaning that they prioritise their human rights due diligence. For example, banks may distinguish between 'low', 'medium' and 'high' risk clients. When a client falls in the latter category, banks will regularly assess whether it complies with the banks policies.
Although the retail sector is an important part of the cocoa value chain, no bank has classified it as a high-risk sector because of cocoa specifically. For one bank, retailers fall under the manufacturing policy when they sell private label products. Like banks, retailers are part of numerous value chains - some of which can be associated with human rights risks. The power of retailers over the cocoa chain is not to be underestimated. Retailers have also played an important role in the increased supply of socially responsible cocoa products.

Dutch retail and industry

Because of its strategic position in cocoa trade and processing, the Dutch retail and industry is strongly committed to promote certification in the cocoa sector. Already in 2010, over 25 retailers, chocolate producers and NGOs signed a letter of intent initiated by the Dutch Ministry of Agriculture, Nature and Food Quality (LNV) and IDH, ensuring that 100% of cocoa consumption in the Netherlands would be certified by 2025.

4.2 How do banks address impacts? (Or how can banks effectively address impacts?)

Risks: due diligence on clients in the cocoa sector

All banks have a sustainability risk framework to assess the commitment, capacity and track record of clients in the cocoa sector. ABN AMRO, ING and Rabobank conduct sustainability assessments of clients during the onboarding process and during annual client reviews. Banks use information provided by their (prospective) clients and information that is available in the public domain. This includes, among other things, reports from NGOs and media articles. A bank's interaction with each of its clients varies. The duration of the relationship or the existence of any particular impacts determine the extent of engagement banks have with their clients. This may take the form of questionnaires, calls or face-to-face meetings to discuss human rights issues. ABN AMRO has defined a list of minimum requirements and benchmark criteria specifically for cocoa, but this does not mean that a client assessment is a 'checklist' exercise. At the same time, while ING's and Rabobank's policies are less detailed, assessments are not necessarily less strict. Indeed, Rabobank is currently the only bank who has published about an ongoing engagement in the cocoa sector, though it does not specify in which part of the value chain the client is active. The case concerns the 'child labour versus poverty dilemma'.

> *For more than a decade (Dutch) banks have been undertaking human rights due diligence in the context of their financing activities for clients in the cocoa value chain, guided by their Environmental and Social Risk (ESR) frameworks. These frameworks have been strengthened over time to reflect developments in industry practice, certification schemes, and the UN Guiding Principles on Human Rights. Dutch banks focus on local processors and traders who are closer to the production part of the cocoa value chain. The appropriate human rights due diligence therefore varies depending on the nature of bank-client relationship, the type of banking facility, the client's size and position in the supply chain, the geographical context of its operations, and the severity of potential adverse human rights impacts. There are many similarities in the approach of the Dutch banks, but there is also scope for further learning from each other's due diligence practices and experiences.*
> Monika Veric, ING, member of the DBA Value Chain Working Group

Considerable similarities as well as some differences were identified among banks as it relates to their approach to definitions of risks, as well as the standards by which they assess their clients. The divergence includes:
- levels of specificity of policies, including for clients in the cocoa chain;
- extent to which analysis of salient issues and root causes informs policies;
- scope, type and depth of questions posed to clients in the cocoa chain;
- engagement with clients on a trajectory towards a sustainable cocoa chain;
- mechanisms applied by banks to take (human rights) due diligence beyond direct clients;
- scope and type of impact that banks focus on in their due diligence (which human rights violations; to what extent root causes are included; what follow-up is given to clients);
- methods to differentiate, assess and incentivise clients through the due diligence process.

How these activities contribute to a sustainabe cocoa supply chain

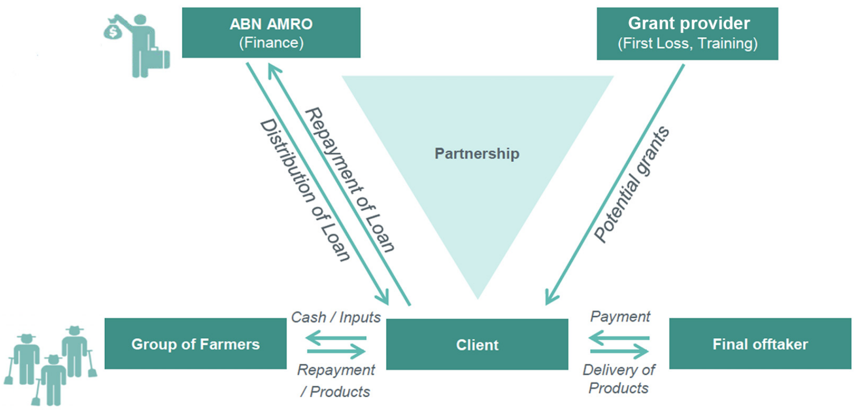
Dutch banks are linked to the situation of cocoa farmers through their bank-client relationship, with for example traders and manufacturers. Therefore, higher standards or 'better' due diligence adds to the alleviation of adverse human rights impacts. The intended effect of banks' efforts is to challenge clients that operate closer to these impacts to raise the bar and push for improvements. However, in the bank-client relationship it is in most cases challenging to attribute actions of the client to the leverage that the bank exercised by engaging with the company. This does not alter the importance of banks' due diligence.

Smallholder finance

Smallholder cocoa farmers experience poor access to finance and high interest rates due to relatively high transaction costs, (perceived) high risks and poor information on past financial performance. In addition, the financial services in cocoa producing countries are often not tailored to the demand of smallholder farmers and are usually not apt for reinvestment of cocoa fields (replanting or grafting of cocoa trees). That is the reason why traders like Olam and Ecom are financing smallholders. However, as their credit needs are increasing, they face liquidity restrictions, so in the long run this turns out to be not a sustainable solution.

Some Dutch banks have started impact finance initiatives, which target smallholders in different agri-commodities. Such initiatives are typically initiated through a third party, which could be a client or financial partner (local bank, cooperative or finance corporation) that is part of the cocoa value chain.
ABN AMRO also cooperates with IDH, the sustainable trade initiative that was founded by the Dutch Government in 2008. IDH aims to convene and co-finance public-private partnerships to unlock investments in a range of commodity value chains and in the apparel sector. IDH has extensive experience in impact measurement. In addition, they reduce the risk on impact finance-projects by taking a first loss on defaulted loans.

Figure 4.1 ABN AMRO example of impact finance initiative with third party



Although impact finance initiatives are on the rise, Dutch banks face a number of challenges. They have no or limited direct presence in cocoa producing countries and no or limited relationships with local banks. Furthermore, smallholder finance has a (perceived) high-risk profile, which diminishes the risk appetite of Dutch banks.

Increasing the size of impact finance programmes, preferably focused on enabling long-term investments, creates a win-win situation as it both contributes to fulfilling the responsibilities under the UN Guiding Principles while at the same time opening up new business opportunities.

The challenges of initiating and expanding programmes for impact finance, may provide room for cooperation and exchange between banks, but also between banks and regulators, or between banks and civil society organisations.

Mutual capacity building

In addition to financing smallholders, some banks provide advisory services to farmers, local cooperatives, clients and other partners. This may include local banks. FMO is working with Ecom to develop and test Key Performance Indicators (KPIs) that measure impact on smallholder livelihood. Rabo International Advisory Services, a subsidiary of Rabobank, helps establishing and professionalising cooperatives, for example by introducing mobile banking services. ABN AMRO's Social Impact Fund has a private equity participation in a company that has worked on the improvement of business skills of leaders in cocoa cooperatives in Ivory Coast. Risk managers of the bank helped implementing this project. Similar work is done by international NGOs, professionalising farmer organisations in relation to access to finance and reducing the risks of banks or other financers.

How these activities contribute to a sustainable cocoa supply chain

Given the huge shortage of capital for smallholders farmers, it can be assumed that every effort to increase access to finance is a step in the right direction. However, experts caution that the need for long-term investments to enable replanting is far greater than short-term financing used to buy fertilizers, for example.

4.3 What are other relevant initiatives in the cocoa value chain for banks to consider?

Certification and traceability

Currently, major voluntary standards are being applied in the sector include Fairtrade, Organic and RA/UTZ. Between them, they have attracted or enabled 100% compliant sourcing commitments by 2020 from four of the top-6 manufacturers: Mars, Hershey's, Ferrero and Lindt. The International Trade Center (ITC) estimates that in 2015, 23% of the global production area was certified by one of the three major labels compared to 11% in 2011. Other companies are choosing to develop their own in-house sustainability programmes, such as Mondelēz's Cocoa Life programme, for example. Although it can be applauded that companies take direct ownership of their sustainability efforts, critics raise concerns around transparency and reliability of reporting.

How these activities contribute to a sustainable cocoa supply chain

These efforts can be looked at in two different ways. On the one hand, it is not possible to offset non-compliance with the UN Guiding Principles by 'doing good' through other initiatives. The UNGPs are concerned with the question how companies make money, not how they spend it. On the other hand, active participation of bank employees who are involved in credit and risk processes for cocoa clients enables them to build a more comprehensive understanding of the sector. A relationship manager would normally visit the corporate headquarters to meet the company treasurer. Engaging with smallholder farmers and cooperatives on the ground is important to build knowledge on human rights risks and impacts.

Triodos Bank—through the Triodos Sustainable Trade Fund—is the only Dutch bank that has a commitment to finance only certified cocoa beans. The other banks' trade finance facilities are not limited to certified cocoa flows. However, banks may temporarily own cocoa stocks when their clients make use of repo services. When this concerns certified stocks, the bank thus becomes part of the chain of custody. For this reason, Rabobank, its subsidiary Rabo Trading Germany and Icestar (a subsidiary of ABN AMRO) are Rainforest Alliance/UTZ-certified. This prevents a bank from being an obstacle in the quest towards increasing certified trade flows.

In 2014, with the objective to combine efforts for sound development of the international cocoa value chain, a multi-stakeholder process was initiated to create a common cocoa standard. This standard is being developed under the ISO system. In fact, the ISO 34101 standard will include specifications for cocoa production, but also for the processing of cocoa as well as business-to-consumer claims. The ISO 34101 standard is designed to: (1) promote good agricultural practices at production level; (2) to improve the social conditions and livelihood of producers; and (3) to protect the environment at different stages of the chain. This ISO standard aims to unify the various certification initiatives and social claims currently used in the value chain.

Certification dilemmas

Certification is not a panacea. The 2017, the Nestlé Child Labour Report stated that the company's initial strategy was to use Fairtrade and UTZ audits to monitor its supply chain. It experienced a lack of support on the ground, which led to concealing child labour during audits. Part of Nestlé's chocolate products is certified by an external body.

Another problem with certification is that most money is made by retailers instead of farmers. This is caused by margin escalation: a small increase in the farm-gate price translates into higher prices for all actors in the value chain, as they seek to maintain the same percentage of added value. This problem could be solved when supply chains are fully transparent, thus allowing the manufacturer to directly pay farmers. This model is being adopted amongst other by Tony's Chocolonely.

Certification bodies themselves face a dilemma: do they focus on increasing market-share or do they push the standard higher? An issue like living income is currently not integrated into certification standards. Paying a living income would help alleviate the root causes of adverse human rights impacts. But it may also raise the price of certified cocoa to a level that certain companies and consumers do not accept.

Industry initiatives

There are two main industry initiatives in the cocoa sector: the World Cocoa Foundation (WCF) and the International Cocoa Initiative (ICI). The WCF has over a hundred members, mainly from the trading, processing and manufacturing stages of the cocoa value chain. It has programmes in Africa, Southeast Asia and the Americas, focusing predominantly on productivity and climate smart agriculture.

The ICI is a multi-stakeholder initiative. Its membership is smaller than the WCF. Apart from the large multinationals, the board includes civil society organisations, such as Save the Children and Solidaridad, and is advised by the International Labour Organization and UNICEF. The ICI develops and implements Community Action Plans, which are predominantly focused on child labour, education, health and rural development. Whereas the WCF focuses on the production stage, the ICI takes a more holistic value chain approach.

> *Throughout the years (Dutch) financial institutions have been actively involved in multi-stakeholder initiatives -sometimes even part of the inception- that aim to increase sustainability in specific supply chains. The Round Table for Sustainable Palm Oil, which brings together representatives from amongst others, civil society, financiers, growers, traders and manufacturers is a clear case in point. But so are roundtables that focus on responsible soy production and the Global Roundtable for Sustainable Beef. Although operating with varying degrees of uptake, all of these initiatives share that they offer a platform to help bring about real change on the ground.*
> Maarten Biermans, Rabobank, member of the DBA Value Chain Working Group

There are many other initiatives in the cocoa sector addressing sustainability. Some are private, some public and others are public-private. Certain initiatives are at global level, while some are at national level. Some focus on overall cocoa production; others on social conditions in the cocoa chain or on deforestation. However, these initiatives tend to be scattered, diverse and incapable of leveraging a multi-stakeholder force for change. In other sectors, multi-stakeholder initiatives at global level have enabled systemic change towards sustainable value chains, such as in palm oil (Round Table on Sustainable Palm Oil), soy (Round Table on Responsible Soy), rice (Sustainable Rice Platform SRP) and in aquaculture (the Aquaculture Stewardship Council ASC). Moreover, the role that banks can play and the leverage that they may have, is not used in the cocoa chain initiatives so far, unlike the RSPO for example.

Although it might be too early to conclude that the cocoa sector needs a (global) multi-stakeholder initiative that involves banks, experience from other industries suggests that it is worth exploring.

4.4 New initiatives to be considered?

ESG-incentives through loan pricing

In June 2017, the revolving credit facility (RFC) (i.e. balance sheet financing) of Barry Callebaut was amended to include an ESG-incentive. ING was the syndicate leader in the deal, and both ABN AMRO and Rabobank participated. The credit rate to be paid by Barry Callebaut was tied to the company's sustainability performance as measured through its Sustainalytics rating. The loan included a 'margin discount' and a 'margin premium', which is applied when Barry Callebaut's score would increase or decrease. Sustainalytics evaluates companies' ESG performance according to a comprehensive methodology, though it is primarily based on public information. This year also Olam has closed a RCF with an ESG incentive where ING led and ABN and others participated.

5 Recommendations

This chapter contains the recommendations that were developed and agreed upon by the working group, based on the outcomes from the value chain analysis. These recommendations are directed at all covenant parties and will be considered by the steering committee of the DBA.

1. Strengthening due diligence by banks that finance the cocoa sector

What gap has been identified?

Public policies and due diligence practices regarding the cocoa sector are diverse amongst Dutch banks. This divergence includes:

- Levels of specificity of policies, including for clients in the cocoa chain.
- Extent to which analysis of salient issues and root causes informs policies.
- Scope, type and depth of questions posed to clients in the cocoa chain.
- Engagement with clients on a trajectory towards a sustainable cocoa chain.
- Mechanisms applied by banks to do (human rights) due diligence beyond their direct clients' operations (supply chain actors further upstream).
- Scope and type of impact that banks focus on in their due diligence (which human rights violations; to what extent root causes are included; what follow-up is given to clients).
- Methods to differentiate, assess and reward clients through the due diligence process.

What is the opportunity?

Despite the divergence in approaches outlined above, banks are keen on enhancing their existing due diligence practices and mechanisms for application in the cocoa chain. Therefore, there is an opportunity to:

1. Engage in an exchange of due diligence systems and practices.
2. Draw lessons learned and formulate good practices for application in the cocoa value chain.

Recommended action

Organise a series of exchange sessions on due diligence practices and mechanisms. Preferably, sessions including experts from all covenant parties, commercial colleagues in banks as well as selected clients and stakeholders in the cocoa sector. The focus is on the role financial institutions can play in creating positive change in the cocoa chain, using their leverage when engaging with other actors in the value chain, from retailers down to producing organisations.

What could be the role of the parties?

- Lead: One bank to take the lead in coordinating the series of sessions.
- Banks: It is critical that banks ensure the involvement of commercial employees and invite some of their clients (at least for a few sessions).
- Other covenant parties: Government, unions and civil society will actively participate involving their financial and cocoa experts, thus providing external advice on the banks' due diligence.

What are the expected outcomes?

- Banks strengthening their policy commitments and due diligence processes, based on good practices and lessons learned from exchange within the banking sector.
- Banks communicating their due diligence process more explicitly to cocoa clients.
- Banks applying their due diligence process in the cocoa chain with integrated mechanisms for positive incentives (including differentiated finance conditions), risk and priority assessment on human rights violations, grievance and corrective action.
- Government, unions and civil society playing their complementary role in advancing and stimulating due diligence by banks.
- Publication of lessons learned and good practises to the benefit of the wider financial sector.
- Banks engaging with local banks and sharing good practices to improve the due diligence process of local banks.
- Banks and other chain actors effectively using their leverage over retailers, manufacturers and traders to encourage a reduction of human rights violations in the cocoa value chain.

What is the proposed timeline?

A series of sessions on due diligence is planned to be held in the August – December 2018 period.

2. Improving access to finance for cocoa reinvestment by smallholders

What gap has been identified?

Smallholder cocoa farmers experience poor access to finance and high interest rates due to relatively high transaction costs, high risks and poor past financial performance. In addition, the financial services in cocoa producing countries are often not tailored to the demand of smallholder farmers and are usually not apt for reinvestment of cocoa fields (replanting or grafting cocoa trees).

Some Dutch banks have started impact finance initiatives, which target smallholders in different agri-commodities. Such initiatives are typically undertaken through a third party, which could be a client or a financial partner (local bank, cooperative or finance corporation) that is part of the cocoa value chain. However, these banks face a number of challenges with such initiatives:

- Dutch banks have no or limited direct presence in cocoa producing countries and no or limited relationships with local banks;
- Smallholder finance has a high-risk profile, which diminishes the risk appetite of Dutch banks.

Despite these challenges, banks are willing to explore how to improve access to finance for cocoa smallholders.

What is the opportunity?

With all knowledge gained through the DBA and its value chain working group, several opportunities emerge:

- Continuing to facilitate the learning amongst DBA parties through the organisation of joint sessions on impact finance;
  - Exploring opportunities for collaboration between DBA parties and – where relevant – including initiatives, such as Root Capital, Alterfin, Incluvest and the Innovative Finance Initiative. The latter is convened by IDH, the Sustainable Trade Initiative, and intends to catalyse the financial industry and the supply chain to improve access to finance for cocoa smallholders while addressing human rights impacts.

Recommended action

- Organise regular meetings to stimulate collective learning amongst DBA parties on impact finance and smallholder finance, also involving relevant initiatives.

- Explore opportunities to further enhance collaboration between the DBA parties and relevant existing initiatives aimed at smallholder finance in order to improve access to finance for cocoa producers and to address human rights impacts.

What is the role of the parties?

- Lead: One of the DBA parties will coordinate the above actions.
- Banks: Explore opportunities to collaborate with DBA parties on improving access to finance and addressing human rights impacts. Where relevant they consider participation in existing initiatives, such as the Innovative Finance Initiative which is convened by IDH, to improve access to finance for cocoa smallholders. In addition, banks' impact finance teams participate and discuss in a joint meeting (within the boundaries of competition law) the barriers they experience or expect regarding impact financing and how these barriers may be overcome in cocoa.
- Other covenant parties: Civil society organisations in the DBA share their work on improving access to finance to address human rights impacts and explore opportunities to collaborate with banks. The Ministries of Finance and Foreign Affairs support the joint meeting (and possibly host it). Government, unions, civil society and others will provide their expertise, experience and insight on the current failure of the local financing system in reaching cocoa smallholders and how to address it. In particular, they help crafting an appropriate and viable role for Dutch banks given that they have little presence in the cocoa producing countries.

What are the expected outcomes?

- Banks and civil society organisations in the DBA design a methodology to collaborate on improving access to finance and address human rights impacts.
- DBA and individual parties engage in relevant existing initiatives, such as the Innovative Finance Initiative which is being convened by IDH – the Sustainable Trade Initiative.
- By doing so, banks engage in impact finance to the cocoa chain.
- Banks design financial products and services targeted at, and tailor-made for cocoa smallholders that includes addressing human rights impacts.
- Government, unions and civil society play their complementary role in enabling impact banking and designing tailor-made products and services.
- Publication with lessons learned and insights to the benefit of the wider financial sector.

What is the proposed timeline?

- Exploring and designing a methodology to collaborate: August 2018 to March 2019.
- Outreach to relevant initiatives is organised by August 2018.
- A meeting for collective learning organised by December 2018.
- Analysis of experiences by banks engaging in impact finance presented by December 2019.

3. Advancing a multi-stakeholder approach towards sustainable cocoa

What gap has been identified?

There are many initiatives in the cocoa sector addressing sustainability. As outlined in Chapter 4.3, these initiatives tend to be scattered, diverse and do not reach a multi-stakeholder force required for sectoral transformation. In other sectors, multi-stakeholder initiatives at a global level have contributed to systemic change towards sustainable value chains, such as in palm oil (Round Table on Sustainable Palm Oil - RSPO), soy (Round Table on Responsible Soy - RTRS), rice (Sustainable Rice Platform - SRP) and in aquaculture (the Aquaculture Stewardship Council - ASC). Moreover, the role that banks can play currently seems underutilised in cocoa value chain initiatives.

What is the opportunity?

The collaboration of parties in the DBA and the value chain working group in particular, is in some ways unique because of its multi-stakeholder composition and its focus on how Dutch banks can contribute to promoting and safeguarding human rights in the cocoa value chain. There are many existing initiatives in the cocoa sector, but their impact could be further enhanced by setting a common agenda to address the sustainability challenges that undermine the sector's long-term prosperity. Against this backdrop, this DBA working group would like to conduct an analysis of the existing cocoa initiatives as an investigation on ways to build bridges between these initiatives. This analysis is expected to result in a set of clear recommendations for a multi-stakeholder framework that aims to connect existing cocoa initiatives. By doing so, the DBA can apply the leverage of Dutch banks and their clients throughout the cocoa value chain to prevent and mitigate human rights violations in the cocoa sector.

Recommended action

- Analyse existing initiatives in the cocoa sector and their contribution to prevent, mitigate and remediate human rights violations.
- Explore options for a multi-stakeholder approach connecting forces of existing initiatives towards systemic changes in the cocoa sector.

Further context to this recommended action

It is recommended to facilitate a series of interviews, discussions and meetings with representatives of existing cocoa initiatives in order to analyse the contribution of the current initiatives and explore how the financial sector could offer added value. On that basis, potential ways for building bridges and unifying forces are identified resulting in a set of recommendations for a new multi-stakeholder framework (provided there is sufficient demand for such an approach).

Such a new multi-stakeholder framework has some clear preconditions:

- The role of banks and their leverage is pivotal.
- It includes producer organisations, traders, authorities, manufacturers, retailers, certifiers, cocoa experts, civil society organisations, trade unions and other value chain actors.
- Representation from global level down to national level in cocoa producing.
- as well as processing countries (such as Ghana, Ivory Coast and Indonesia, but also The Netherlands as a country with a relatively high cocoa processing and manufacturing capacity).

What could be the role of the parties?

- Lead: This multi-stakeholder approach will be led by a small multi-stakeholder coalition: a Dutch bank will take the lead on this analysis; the Dutch Government will request its agricultural experts to contribute to the analysis; civil society organizations will also deploy a person with ample practical experience in multi-stakeholder processes and platforms.
- Banks: Banks will play a critical role in ensuring relevant employees perceive its value and participate in the analysis and evaluation of the recommendations. Moreover, it will be critical that banks are open to recognise and reflect on their role in the cocoa value chain, as well as advancing the importance of addressing sustainability in cocoa in a multi-stakeholder setting.
- Other covenant parties: Civil society organisations (CSOs), government agencies and trade unions are all important actors and participate in the analysis. The civil society partners are well placed to build on lessons from other multi-stakeholder initiatives. One CSO with the support of others will coordinate the

series of meetings. The Dutch Government through its Embassies in Ghana and Indonesia will facilitate the series of meetings in these countries. Meetings in The Netherlands can be convened by the Ministry of Foreign Affairs and/or Economic Affairs.

What are the expected outcomes?

- Analysis of existing cocoa initiatives and possible added value the DBA could offer disclosed and disseminated in a report.
- Recommendations for multi-stakeholder action towards a sustainable cocoa chain (framework to connect existing initiatives; settings; national versus supra-national level; facilitation; topics for discussion; scope of action; expected impact; critical success factors).
- Recommendations for banks and financial institutions in such multi-stakeholder action.

What is the proposed timeline?

The analysis report is presented by February 2019.
The recommendations for a new multi-stakeholder approach in cocoa will be presented by June 2019.

Annex

Methodology used for the Value Chain Mapping Exercise

Shift

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About the Value Chain Mapping methodology

As part of its support to the value chain mapping working group of the Dutch Banking-sector Agreement (DBA), Shift was asked to develop a methodology in line with the UN Guiding Principles that could guide and structure the value chain mappings of the working group.[1] The methodology builds on and recognizes individual responsibilities of banks, while seeking to benefit from the knowledge and expertise of the multi-stakeholder parties in the DBA and the working group.

Value chain analysis is a tool designed to understand connections of companies to potential human rights impacts, identify gaps in how they are being addressed, seek opportunities for leverage and devise preventative and mitigating actions. In the methodology below these are presented in a series of logical process steps (A, B, C, etc.) with each looking at a number of sub elements (A.1, A.2, A.3, etc.) and commensurate questions to trigger and guide thinking to realize these objectives.

Methodology Value Chain Mapping Exercise

#	Sub element	Key Questions
A	**Analyzing the value chain (separate from banks' involvement)**	
A.1	**Value chain - products and services involved**	• What products or services are produced/ generated through the value chain and what are the key steps that make up the value chain?
A.2	**Value chain – entities involved**	• Who are the actors in the value chain? What activities do they conduct? What do we need to know about them for a meaningful analysis?
A.3	**Contextual factors**	• What contextual factors in the value chain give rise to heightened human rights risk?
A.4	**Human rights impacts in the value chain**	• What are generically the known risks in each part of the value chain and what is their severity and likelihood? What are their root causes?
A.5	**More information needed?**	• What additional information is needed to complete the analysis?
B	**Mapping banks' involvement with the value chain**	
B.1	**Financing needs**	• What are generally the financing needs and methods in each part of the value chain for the various actors?
B.2	**Products and services**	• What are the products and services that banks offers to entities in the value chain?
B.3	**Business relationships**	• What is the nature (e.g., long term vs. incidental) of the client/business relationships banks have with actors at key parts of the value chain?
C.	**Understanding connection of banks to impacts**	
C.1	**Position of clients in the value chain**	• At which key steps in the value chain are banks' clients operating and what is the nature of their business relationships?
C.2	**Relationship between banks' clients and negative impacts**	• How are clients involved with potential human rights impacts in their own activities or through their business relationships?
C.3	**Linkage between banks' products or services and negative impacts**	• How are the banks' products or services potentially connected to the client's involvement with human rights impacts?

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D.	**Mapping and evaluating existing approaches**		
D.1	**Clients' existing human rights due diligence**	•	What systems and approaches do banks' clients generally have in place to address negative human rights impacts? How effective are they in preventing or otherwise addressing impacts in line with the UNGPs and OECD Guidelines?
D.2	**Banks' existing human rights due diligence**	•	What human rights due diligence measures do banks currently have in place in relation to its clients? How effective are they in preventing or otherwise addressing impacts?
D.3	**Other relevant initiatives**	•	What other human rights initiatives in the value chain that address human rights risks in line with the UNGPs and OECD Guidelines exist? How effective are they in preventing or otherwise addressing impacts?
E	**Identifying additional opportunities**		
E.1	**Prioritization**	•	Based on **severity** (scope, scale and any barriers to remediating an impact, if it were to occur) and (as secondary factor) **likelihood**, which impacts should be prioritized?
E.2	**Using Leverage**	•	What leverage do banks have with entities in the value chain to prevent and mitigate impacts and how can they best use it?
E.3	**Increasing leverage**	•	How could banks increase their leverage for human rights purposes over relevant entities?
E.4	**Terminating a relationship**	•	Under what circumstances should a bank consider exiting a relationship, and what factors should it take into account in any such decision?
F	**Drawing conclusions and recommendations from the analysis**		
F.1	**Prioritization**	•	Which issues should banks (individually and/or collectively) focus on? Which client relationships should they prioritize? What other priorities should they set?
F.2	**Applying leverage**	•	What are the additional options for exercising/increasing leverage by banks and how might they contribute to a reduction of severe human rights impacts in banks' value chains?
F.3	**Stakeholder engagement**	•	How could banks engage with affected stakeholders about their efforts in addressing human rights impacts in the particular value chain?
F.4	**Output and outreach**	•	What would the best way to share lessons learned and reach parties who could benefit from the analysis? How could the results from the analysis be presented and/or launched?

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