

Supertrends

Supertrend Climate Change – Feeding the world sustainably

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Global food production accounts for between 25%-30% of global greenhouse gas (GHG) emissions, according to the Intergovernmental Panel on Climate Change (IPCC). Indeed, the agricultural sector can be singled out as the largest driver of environmental planetary change (Steffen et al., 2007).

Humankind must also grapple with another enormous food-related challenge. Every day, some 800 million people go to bed hungry, according to the Food and Agricultural Organization of the United Nations (FAO). Supply is not the problem, but instead low incomes, lack of access and wasteful supply chains. And with incomes and the global population projected to increase, food demand will rise another 60%- 110% by 2050 (Pardey et al., 2014). This leads to a critical question: how to transform the agricultural sector so that it can feed the world and also contribute to slowing climate change.

This research alert explores how sustainable intensification of agriculture can be implemented, and which companies stand to benefit from this transformation. First, on the production side, boosting yields of crops and livestock through sustainable intensification can have a big impact on GHG emissions by reducing emissions per unit of food produced. Second, from a consumption perspective, advancements can be made by reducing food waste and by shifting diets away from emission-intensive products like beef and toward plant-based foods. The two main pillars of GHG emission reductions in agriculture are covered in this report.

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■ BUY

Stocks related to the Climate Change Supertrend in the Subtheme Agriculture & Food

We maintain our conviction on Agco, BRF, Bunge, Danone, Deere and Nestle. We add FMC, China Everbright International and Kerry to our stock list. We replace Charoen Pokphand Foods and Corteva, which had a positive stock price performance since their addition.

The miracle maker

For a long time, the agricultural sector has produced miracle after miracle. Back in 1798, the British economist Thomas Malthus famously theorized that population growth could, if unchecked, outpace agricultural production, leading to mass starvation. Fortunately, this scenario never materialized as both fertility rates fell and food production surged. In the 20th century alone, agricultural yields doubled per hectare, leading to an ever-increasing supply of food (Montgomery, 2017). This development was largely driven by the Green Revolution that began in the 1960s. It describes the production shift in agriculture where intensive farming methods, such as the use of fertilizers and industrial machinery, were widely adopted. A direct consequence of the industrialization of agriculture

were falling food prices, averaging -1% per year in the last 100 years. However, as every investor knows, there is no such thing as a free lunch.

Greenhouse gas emissions on the rise

The positive yield improvements were driven in part by shifting the true production costs onto the environment. The Green Revolution produced one externality after the next. For example, 91% of land deforested since 1970 in the Amazon Basin is used for livestock pasture. Within the agricultural industry, animal agriculture and changes in land use are responsible for the largest share of GHG. The adverse effects of agriculture on the environment have left the sector in a dire situation. Practices that have proved effective over centuries are being questioned from an environmental perspective. Simply increasing acreage for production is difficult, due to limited accessibility. It is also challenging for the sector to irrigate crops, as water resources dwindle in key farming areas around the world. Furthermore, a third of all agricultural soil globally is degraded. Soil management is a practice that was sidelined by conventional farming methods and the result is that more and more soil is being eroded or degraded. Finally, the sector's reliance on fossil fuels, deforestation, carbon-intensive fertilizers and inefficient manure management has made it one of the most GHGs-intensive industries worldwide. As an example of agriculture's resource intensity, for every calorie consumed in the USA, the equivalent energy of 13 calories of oil is burned to produce it.

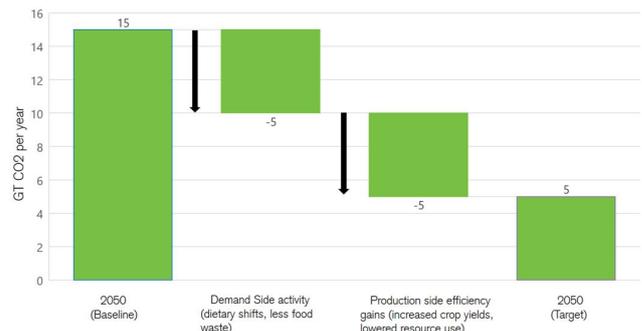
In a hypothetical scenario, with little to no climate action in the agriculture sector, greenhouse gas emissions from agricultural production could increase 58% by 2050 (World Resources Institute). And while agriculture faces mounting challenges to reduce its environmental footprint, the issue of hunger is still not solved worldwide. It appears that the UN could fail to achieve its Sustainable Development Goal of zero hunger by 2030 (FAO). The two issues of hunger and climate change are closely interrelated and need to be solved accordingly. Unaddressed climate change is increasingly affecting yields and rural livelihoods, while food and agricultural systems, as well as the economy at large, continue to emit GHGs. While the situation appears dire, there is a pathway out of this difficult situation for humanity.

Sustainable intensification of agriculture

Business as usual in agriculture is no longer an option, and the concept of sustainable intensification of agriculture is gaining traction. It is the idea that "humanity adopts practices along the entire value chain of the global food system that meet rising needs for nutritious and healthy food through practices that build social-ecological resilience and enhance natural capital within the safe operating space of the Earth system," (Rockström et al., 2017). The necessary shift towards sustainable intensification of agriculture will increase yields, but with less resources and fewer GHG emissions. The aim is to design multi-functional agro-ecosystems that are both sustained by nature and sustainable in their nature. The FAO says that the best way to support this development is by facilitating adequate investments, otherwise technical changes in food and agricultural systems will not lead to

sustainable productivity improvements. Our Climate Change Supertrend identifies companies that follow the trajectory of sustainable intensification of agriculture. To underline that the strategy of sustainable intensification can work, advanced agricultural technology might have the potential to increase farm yields to up to the 70% higher requirements by 2050 estimated by the FAO. In conclusion, the transformation to sustainable intensification of agriculture is justified both by necessity and by opportunity. Humanity needs to safeguard global sustainability, which is a precondition for long-term agricultural viability, but also use sustainable practices as a vehicle for a second green revolution.

Figure 1: GHG emission reduction targets



Source: World Resources Institute, Credit Suisse

Technology at the service of human

Precision agriculture (PA), using automation at every productive step, is making farming more efficient, leading towards the goal of securing sustainable global food security. Improved fertilizer, soil and water management can significantly reduce climate gas emissions while maintaining similar yields and reducing production costs. AGCO estimates farmers' savings turning into a USD 80 bn opportunity globally from its suite of PA products.

While Deere has been investing in PA for over twenty years, the creation of a separate unit, Intelligent Solutions Group (ISG), along with the acquisition of Blue River Technology for USD 305 m in 2017 has propelled it to take the lead in PA. Unlike its peers, the company has adopted a unique strategy to develop its enabling technologies, telematics, digital solutions and electrification on a standalone basis. On the other hand, AGCO and CNH Industrial have relied upon partnerships and joint ventures to remain in the race. The next generation of PA is being taking place through the three steps of automation, data sharing and plant level management. As we discuss these steps below, it is evident that while the progress in the first two fields is progressing well, incorporating machine learning into plant-level management will be a next-generation development.

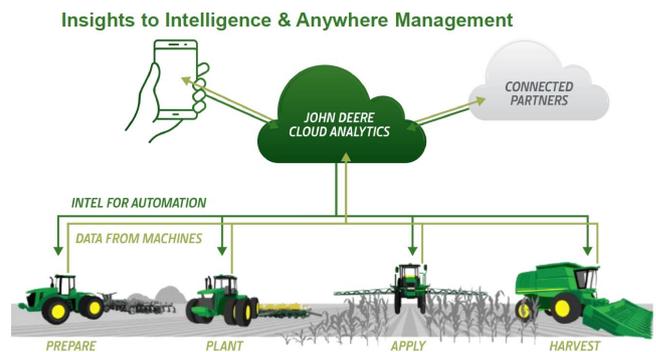
Before fully autonomous farming vehicles can be achieved, it is important to automate every task in farming. In farming today, the primary field sensors are still the farmer's eyes, and the decision-making capabilities are based on the years of a farmer's experience. Movement of equipment happens by hand as the farmer adjusts for in-field conditions. Compa-

nies are changing this dynamic by empowering farmers to automate their tasks. Through sensors and computer vision, the machines can detect both agronomic and machine conditions simultaneously. And through advanced algorithms, they can then process millions of sensor measurements and images to make the optimal decision. As a result, the machines can automatically execute without any intervention from the farmer.

Data is becoming the most critical element in increasing economic value on the farm. Access to better data empowers farmers to make more profitable and sustainable decisions. At 165 million engaged acres globally (compared to 100 million acres in 2018), the John Deere operation center is the largest data platform in the industry connecting devices with the cloud. Deere has built its ecosystem into an open digital platform, which connects over 150 software companies integrated into its platform through Application Programming Interfaces (APIs). An open platform allows for third-party advisers to write agronomic prescriptions that can be pushed back to the cloud and then wirelessly transmitted to machines. Similarly, AGCO's partnership with Bayer can enable its customers to connect with the Climate Corp Field View system to integrate machine data. Fuse, which is AGCO's precision agriculture unit, focuses on delivering connectivity, sensors, machine control, and actionable insights to customers that could enhance farmers' profitability by 20%.

Achieving plant-level management through a combination of data and automation advancement will be the true success for PA. A single cornfield may have as many as 8 million individual plants. This means optimizing the microenvironment around each plant so that farmers realize higher value and outcomes with fewer fertilizers, herbicides and less fuel emissions. This is essential to making agricultural practices more sustainable for the future. Companies are on the cusp of integrating machine learning, AI, and computer vision into their technology, which should help achieve plant-level management and ensure sustainable value creation for generations of equipment. A good example is See and Spray by Blue River Technology, expected to commercialize in 2021, which uses computer vision and advanced algorithms to distinguish between crops and weeds, and then selectively sprays weeds only, enabling a 90% reduction of herbicides in some cases. PA companies anticipate that customers will increasingly adopt these technologies, either through the introduction of new models with increasingly integrated technology or through selecting premium features as an add-on which helps the profitability and positioning over the long-term.

Figure 2: Technology in the fields



Source: Deere, Credit Suisse

Planting for tomorrow

Within the seeds and crop protection or chemical agriculture sector, many small innovations and technologies are helping the world move toward more efficient and sustainable agriculture, albeit at a slow speed as they are adopted. We can see in Figure 3 how land use for cereal has stayed constant while crop yield shot up over the decades. Farmers increase crop yields partly by using better seeds and partly by better management (e.g. fertilizer, pesticides, herbicides, soil). Regulators are also pushing for change with the European Union's "From Farm to Fork" initiative, targeting a reduction of 50% in pesticide use, as well as a 20% reduction in fertilizer use.

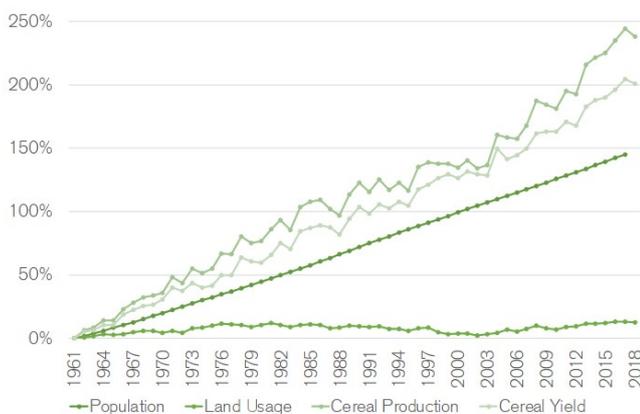
On the seed side, the trend has been to increase yields through enduing seeds with more favorable traits, be it through cross breeding selected traits in seeds or Genetically Modified (GM) seeds. This trend is not homogenous in all regions as the EU highly regulates the use of GM seeds. However, in the USA and emerging markets their use is widespread. GM seeds also address the challenge of toxicity of chemicals. Most companies are in the process of phasing out highly hazardous chemicals from their portfolios and GM crops help in this process. For example, GM crops incorporate resistance to pests, eliminating the need for certain pesticides.

Most fertilizer players offer some digital solutions for clients, in order to improve application efficiency. With some 94% of emissions from fertilizing soils coming from nitrogen application, nitrogen production and application is of ever more importance for fertilizer companies. The deployment of new methods has been rather slow as farmers are not willing to pay for these digital solutions. Overall in the long run, farmers will become more tech savvy in digital agricultural technologies. When combined with new methods of application, it will allow for much more precise laying of fertilizers and can reduce fertilizer volumes per hectare used. These methods will also have an impact on fertilizer mix through optimized quantities. A prime example is China, where nitrogen is heavily over used and potash heavily under applied.

Nitrogen losses from inefficient usage of fertilizers not only leads to poor crop productivity but also contributes to environmental pollution. Yara's premium products (nitrate-based crop nutrition solutions) have demonstrated an improved nitrogen usage efficiency when compared to traditional commodity

products. YaraVita is a specialty product applied directly to the leaves for increase in yields. Increased sales of premium products and YaraVita can be treated as proxy for improved nutrient use efficiency. Yara aims to boost sale of both premium products and YaraVita by approximately 26% and 133%, respectively by 2025. Continued innovation is vital for a leading agricultural science company like FMC, which has a world class product portfolio offering crop protection and Plant Health solutions. The products are used for protection against a broad spectrum of insects, weeds, and diseases. FMC continues to develop new molecules to counter pests that have developed resistance to older technologies. To further reduce environmental impact, FMC is developing Biologicals, which are plant protection products derived from microorganisms and other naturally occurring material. These include products like Quartzo and Presence bionematicides, which provide dual benefits of reducing the threat of nematodes and increasing microbial activity in soil.

Figure 3: Agriculture efficiency



Source: World Bank, FAO, Credit Suisse

Change in consumption

Younger generations are mindful of GHG emissions and the impact they have on our planet, and they want to play their part by consuming sustainably produced food. As health is another priority for this group, healthy and sustainable food is on the rise. These consumer trends support the sustainable transformation of the agricultural sector, leading to both reduced GHG emissions and more available food. Critics have increasingly targeted meat as an issue for both the environment and human health. Meat production is responsible for 58% of food-related greenhouse gas emissions (see Figure 4). Separately, the World Health Organization has classified processed meat as carcinogenic to humans, while a 2020 study published in the *Jama Internal Medicine* journal found that the consumption of processed meat, unprocessed red meat and poultry was “significantly” associated with cardiovascular disease.

A 2019 report commissioned by the leading medical journal *The Lancet* developed a “planetary health diet” that aims to improve human health, while ensuring environmentally sustainable food production for a future global population of 10 billion people. The report – a three-year collaboration between scientists in areas ranging from environmental sustainability,

agriculture, political science and health – recommends cutting red meat and sugar consumption, increasing intake of fruits, vegetables and nuts, and adding plant protein to diets. The recommendations also include a shift toward enhanced biodiversity in terms of crops, sustainable expansion of agriculture, reduction of food waste in production and consumption, and stricter rules for protecting oceans. “Food is the single strongest lever to optimize human health and environmental sustainability on earth,” according to the report from the EAT-Lancet Commission.

We are thus seeing the rise of meat and dairy alternatives. The plant-based protein market, helped by the development of increasingly tasty products, has huge potential. In the USA, for example, plant-based milk products account for 13% of the overall milk category, according to a 2019 report from the Plant Based Foods Association. While consumers in the USA and Europe are familiar with these products, the Asian market has yet to be conquered, which should lead to further strong growth. Over the last 12 months, media attention has turned to plant-based meat options, such as burgers or sausages, and if we see a similar development as for dairy products, plant-based meat could conquer 10% of the meat market. Consumers are also pushing for food that is low in sugar and additives. In response, traditional food companies are investing in innovation to alleviate market share losses. Ingredients companies, which are bringing novel solutions to food manufacturers, are well-positioned to benefit from this trend.

The COVID-19 crisis may act as an accelerator of the development of healthy sustainable food, with consumer focus on wellbeing and immunity increasing: Nestle is leveraging this trend with clearer messaging on the packaging of its portfolio of trusted brands. Danone’s dairy business is also directly in tune with this trend. The COVID-19 crisis also offered a unique opportunity for plant-based meat producers to increase their exposure to home consumption. Disruption in meat production due to facility closures led to empty shelves in supermarkets. At the same time, plant-based companies used the opportunity to redirect their business out of the closed restaurant channel to the retail channel, increasing their exposure to the consumer. Kerry is a market leader and a supplier to the plant-based meat industry.

Figure 4: The environmental cost of food production



Source: Poore & Nemecek, Credit Suisse

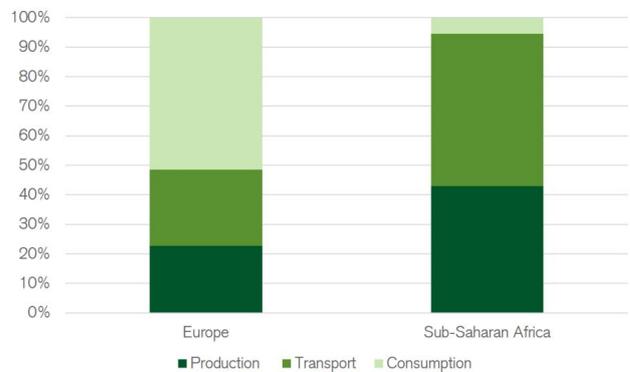
Don't waste it

The FAO has estimated that one third of global food ends up as waste. The reasons behind food waste are complicated. In developing markets, the process is driven by inefficient supply chains and a lack of infrastructure, while in developed countries the majority of food gets lost at the consumer level. The environmental consequences of food waste are dire. According to the FAO, GHG emissions of food waste amounts to 3.3 Gigatons, or 6% of all GHG emissions. If food waste were a nation, it would be the third-largest emitter of GHG emissions after the USA and China. In addition to the GHG emissions released when food decomposes, food waste also poses a risk to global food supplies. Thus, the United Nations has declared the Sustainable Development Goal of halving food waste by 2030. As such, several companies are taking impactful actions to manage and reduce food waste, which indirectly and/or directly benefits their businesses. As part of this report's theme of sustainable intensification of agriculture, food waste is regarded as an externality that can be reduced by companies that profit from doing so.

Food retailers have a wide range of options to reduce food waste. While retailers are only directly responsible for 2% of food waste, their concentrated market power and trading practices drive much of the waste in their supply chain (Colbert, 2017). For example, when a supermarket orders apples and cancels the order at the last-minute due to cosmetic specifications, the apples are usually diverted to a landfill. Furthermore, supermarkets dominate consumer shopping through their marketing practices and influence what consumers buy and how they use it. Actions that can be taken by retailers to reduce food waste include providing transparent food waste data, removing best-before labels as well as easing cosmetic requirements for the products. Ultimately, retailers must have internal policies in place to reduce food waste. Both Tesco and Walmart have pledged to reduce food waste by 2030, in line with the UN's SDG and have a proven track record of tackling food waste (Feedback, 2018). Clients can reward food-waste reduction programs by staying/becoming loyal customers (BCG, 2018).

Directly benefitting from food waste are waste management firms, such as China Everbright International or Cleanaway Waste Management, by using food waste as resources for other commercial uses. This allows them to recycle the resources and energy stemming from inputs for growing food in the first place. Their actions ensure that food waste does not decompose at landfills, where the GHG emissions of food waste are released. China Everbright International, for example, is a company that has several environmental energy projects, including waste-to-power plants and methane-to-power plants. At their Sanya power plant, 200 tons of food waste are processed and incinerated daily. The company is able to produce several new products out of food waste. Biogas and bio-oil are sources of energy, while the remaining dry waste can be turned into sustainable fertilizers. It expects to see strong growth in its WTE (waste-to-energy) treatment capacity, while biomass capacity should also increase given strong support from the Chinese government.

Figure 5: Food waste: Regional differences



Source: World Resource Institute, Credit Suisse

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Stock selection for sub-theme "Agriculture and food"

Name	ISIN	Country	Ccy	CS Rating	Mcap (in USD bn)	PE 2021E (FY)	EPS growth 2021E (FY)	Div Yield 2021E (FY)
AGCO	US0010841023	United States	USD	HOLD	5.3	15.0	26%	0.9%
BRF	BRBRFSACNOR8	Brazil	BRL	BUY	2.9	17.4	96%	1.9%
Bunge Ltd	BMG169621056	United States	USD	BUY	6.6	10.9	26%	4.4%
China Everbright International	HK0257001336	Hong Kong	HKD	BUY	3.8	4.3	14%	6.8%
Danone	FR0000120644	France	EUR	BUY	45.6	15.3	8%	3.8%
Deere	US2441991054	United States	USD	BUY	64.3	19.6	41%	1.6%
FMC	US3024913036	United States	USD	BUY	14.1	14.9	13%	1.9%
Kerry	IE0004906560	Ireland	EUR	HOLD	22.8	27.3	15%	0.8%
Nestle	CH0038863350	Switzerland	CHF	HOLD	347.6	24.2	7%	2.6%

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Source: Bloomberg, Credit Suisse

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Guide to analysis

Absolute stock rating allocation as of (31/08/2020)

Rating	Overall	MiFID Services*	Allocation over 12 months**
BUY	41.74 %	32.55 %	832
HOLD	48.04 %	30.42 %	961
SELL	8.50 %	20.11 %	171
RESTRICTED	1.71 %	65.71 %	29

*Proportion of recommendations per rating category where MiFID services were provided to the issuer over previous 12 months.

**This includes recommendations of issuers where investment firm services have been provided.

Below indications serve as a guide for the meaning as well as the length of time pertaining to an investment recommendation:

Absolute stock performance

The stock recommendations are BUY, HOLD and SELL and are dependent on the expected absolute performance of the individual stocks, generally on a 6–12 month horizon based on the following criteria:

BUY	10% or greater increase in absolute share price
HOLD	variation between –10% and +10% in absolute share price
SELL	10% or more decrease in absolute share price
RESTRICTED	In certain circumstances, internal and external regulations exclude certain types of communications, including e.g. an investment recommendation during the course of CS engagement in an investment banking transaction.
TERMINATED	Research coverage has been concluded.

Absolute bond performance

The bond recommendations are based fundamentally on forecasts for total returns versus the respective benchmark on a 3–6 month horizon and are defined as follows:

BUY	Expectation that the bond issue will outperform its specified benchmark
HOLD	Expectation that the bond issue will perform in line with the specified benchmark
SELL	Expectation that the bond issue will underperform its specified benchmark
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