

3.4 Forestry

3.4.1 What is at stake?

Forests make up 3.9 billion hectares of the earth's surface. Another 190 million hectares is covered by timber plantations, which are often also classified as forests despite fundamental differences in the services the two provide. Combined, trees cover about 4 billion hectares or about 30 percent of the world's land area.⁵⁵

These forests and plantations provide a large variety of services and roles, many of which are mutually exclusive:⁵⁶

- Over 90% of the 1.2 billion people living in extreme poverty depend on forests for some part of their livelihoods. About 350 million forest peoples call forests their home and their economic well-being is inextricably linked to gaining a livelihood from using a variety of timber and non-timber products;
- For many indigenous peoples and forest-dependent communities, forests are home. Forests thus play a very important role in their social and cultural life;
- Forest ecosystems are the most bio diverse terrestrial ecosystems we have, being home to at least 80% of all land-based plants and animals;
- As major carbon storehouses and sinks, intact forests provide invaluable climate protection services. The amount of carbon currently stored in Canada's boreal forests is for instance equivalent to 7.8 years of the world's total carbon emissions in 2000 and has been estimated to be worth US\$ 3.7 trillion.⁵⁷ Yet as greenhouse gas concentrations in the atmosphere increase, forests will be significantly affected by global climate change itself, threatening their capacity to continue sequestering and storing carbon;
- Forests help to maintain the fertility of the soil, protect watersheds and reduce the risk of natural disasters such as floods and landslides by regulating water supplies and stemming soil erosion. These services have an enormous impact on worldwide agricultural productivity and human health;
- The forests product industry is a source of economic growth, providing wood and non-timber forest products such as edible nuts and fruits, medicinal plants, fibres and rubber. The global trade in forest products has an estimated annual value of US\$ 270 billion, of which around 20% is originating from developing countries. The economic importance of the informal and local trade in timber and non-timber forest products probably exceeds this figure dramatically;
- Forestry activities also create employment, but large differences exist between types of forestry activities. Small-scale and informal forestry can be an important source of employment, especially in combination with agroforestry. Large scale plantations, however, generate much less than alternative land uses. In Brazil for instance, timber plantations employ not more than one person per 45 hectares, while agricultural activities give work to at least 18 per hectare.⁵⁸

Yet, forests continue to be destroyed at unprecedented rates. Experts estimate that approximately 16 million hectares of natural forests were lost annually during the 1990s, and deforestation rates have not changed significantly since then.⁵⁹ While not fully deforested, additional large areas of tropical, temperate and boreal forests are also

significantly degraded by over-exploitation each year. Important drivers of deforestation and forest degradation are:

Unsustainable and illegal logging practices occur when forests are deprived of their resources at such a pace and in such a way that regeneration is not possible. Although unsustainable logging practices are often illegal as well, the two categories are not identical. Not all unsustainable logging is illegal, as forestry legislation in many countries is not yet oriented sufficiently on sustainable logging practices. And not all illegal logging, for instance by forest-dependent communities, is unsustainable.

There are many drivers of unsustainable and illegal logging practices, but the establishment of pulp, paper and ply mills which do not have sustainable wood supply plans or procurement systems is a very significant one.

Illegal logging costs governments of timber-producing countries an estimated € 10-15 billion per year in lost revenues, which could otherwise be spent on the provision of better healthcare, education and other public services, as well as the implementation of sustainable forest management.

Unsustainable logging also causes enormous environmental damage and loss of biodiversity, for instance through conversion of bio diverse grasslands or forests to plantations or simplified secondary forests, or through logging in protected areas and along streams. It can also facilitate the illegal exploitation of wildlife.

Unsustainable and often illegal logging thus undermines sustainable forest management and has a long term negative impact on the livelihoods of forest-dependent people, many of whom are amongst the world's poorest and most marginalized people.

In some forest-rich countries, the corruption fuelled by profits from the allocation of concessions and the resulting illegal forms of large-scale logging has grown to such an extent that it is undermining the rule of law, principles of democratic governance and respect for human rights. In some cases this illegal exploitation of forests is also associated with violent conflict.⁶⁰

Conversion of natural forests into timber or pulp plantations to supply the timber and pulp and paper sector. Although these plantations are sometimes classified as forests as well, for instance in the [State of the World's Forests](#) published annually by the *Food and Agriculture Organization of the United Nations (FAO)*, they lack most of the social and environmental qualities of natural forests;

Conversion of forests for agricultural expansion such as cattle ranching and the production of palm oil, soy and grains (for food, agrofuel and other purposes). This subject is treated in more detail in paragraph 3.1 on Agriculture;

Conversion of mangrove forests for aquaculture. This subject is treated in more detail in paragraph 3.3 on Fisheries;

Development of large-scale industrial and infrastructure projects, such as roads, railways, dams, mines and oil and gas installations and pipelines. Some of these subjects

are treated in more detail in paragraph 3.2 on Dams, paragraph 3.6 on Mining and paragraph 3.7 on Oil & Gas.

Deforestation and forest degradation deprive communities of their land and means of living, often cause biodiversity loss, soil erosion and cause surface and ground water levels to fall, often dramatically. Additionally, deforestation activities sometimes cause severe forest fires, such as those in Indonesia in 1997/1998. Because of the air pollution caused by the fires some 40,000 people were hospitalised for respiratory and other pollution-related ailments such as asthma, bronchitis and pneumonia, as well as eye and skin problems. Most of these fires were caused by the expansion of large scale industrial pulpwood and oil palm plantations.⁶¹

Deforestation is also accelerating global climate change. According to the [Stern Review](#) greenhouse gas emissions from deforestation are estimated to represent more than 18% of global greenhouse gas emissions, a share greater than is produced by the global transport sector.⁶²

This paragraph deals with the forestry sector, which comprises all companies managing forests and plantations, as well as the companies processing wood into timber, pulp, paper and other wood products. Additionally, the forestry sector encompasses all companies involved in trading and further processing these products, for instance into furniture.

The forestry sector certainly is not the only economic sector which is involved in and has the potential to help slow global deforestation and forest degradation. Other related sectors such as agriculture, fisheries, dams, mining and the oil & gas are discussed in other paragraphs. The forestry sector deserves a separate treatment as this sector is highly dependent on the state of the world's forests.

However, the forestry sector has often failed to play a constructive role in conserving and managing the world's forest resources. According to a recent [World Bank study](#), "Industrial timber production has a poor track record in Africa. Over the past sixty years, there is little evidence that it has lifted rural populations out of poverty or contributed in other meaningful and sustainable ways to local and national development."⁶³ The [Inspection Panel of the World Bank](#) assessing the World Bank's role in industrial forest management in Cambodia concluded that "one could hardly overemphasize the negative effects of the logging on a natural habitat of world class value and most importantly on very poor and vulnerable rural communities and indigenous peoples."⁶⁴

To be sure that its clients in the forestry sector break with this heritage and manage forests in a way that ensures not only environmental sustainability but also benefits to local communities, banks need to develop a strict policy to screen their clients against. In developing this policy banks should make use of the best international standards available. Some of these are described below.

3.4.2 Best standards available

The most important international standards and initiatives for the forestry sector are:

Land rights of local and indigenous communities

Uncontested land rights and title are a prerequisite for secure forest tenure, just as access to forests and forest resources are prerequisites to sustainable forest management. Various international conventions acknowledge the rights to the fair and equitable use of forest resources by indigenous peoples and forest-dependent communities. The [UN Declaration on the Rights of Indigenous Peoples](#), adopted by the General Assembly of the United Nations in September 2007, affords indigenous peoples right to the lands, territories and resources which they have traditionally owned, occupied or otherwise used or acquired.⁶⁵ This issue is discussed further in paragraph 4.4 on indigenous peoples.

Illegal logging and forest governance

Since 2002, a number of [Ministerial Conferences on Forest Law Enforcement and Governance \(FLEG\)](#) have been organized in the East Asia and Pacific region, Africa and in Europe and North Asia, co-hosted by both producer and consumer governments and the World Bank. A potential FLEG initiative in Latin America and the Caribbean is underway. These ministerial-level political processes aim to mobilize international commitment from producer, consumer and donor governments to increase efforts to combat illegal logging as well as the associated trade and corruption in the forest sector.⁶⁶

In 2004 the European Union adopted the [Forest Law Enforcement, Governance and Trade \(FLEGT\) Action Plan](#) developed by the European Commission in May 2003. The Action Plan sets out a new and innovative approach to tackling illegal logging, linking good governance in developing countries with the legal trade instruments and leverage offered by the EU internal market. The Action Plan describes a package of measures, including encouraging the private sector to adopt purchasing policies to exclude illegal timber from their supply chains and encouraging measures to avoid investment in activities that encourage illegal logging.⁶⁷

Certification of forest management and chain of custody

Most certification schemes developed to guarantee sustainable forest management unfortunately fail to secure balanced decision-making in the development and monitoring of their standards. In most cases this basic failure coincides with the scheme being closely linked to companies active in the forestry sector. In these cases, the schemes only reinforce the *status quo* of unsustainable and often illegal forest management, rather than improving it. This unbalanced representation at the standard setting table is reflected in the widespread failure of most certification schemes to recognise the rights of indigenous peoples and forest-dependent communities to participate in decision-making.⁶⁸

The only certification scheme which deals with this subject in a convincing way is the Forest Stewardship Council (FSC), which represents forest owners, forestry companies, trade unions and social and environmental organizations. FSC has formulated ten [Principles of Forest Stewardship](#). With the associated Criteria these form the basis for all FSC forest and plantation management standards. Over the past 13 years, over 90 million hectares of forests and plantations in more than 82 countries have been certified according to FSC standards while several thousand products are produced using FSC-certified wood and carrying the FSC trademark.⁶⁹

FSC is the only certification scheme consequently supported by all major environmental and development NGOs, as well as many grassroots organisations. However, this support has been tested and will depend on FSC's ability to adapt to new challenges, improve its standards and improve its performance on the ground. Most contested issues at the moment are the Chain of Custody certification and the certification of plantations:

- Apart from certifying forest management, FSC also certifies companies operating in the [Chain of Custody](#) (CoC) of timber and paper products. This certification implies that all or a significant percentage of the wood products used or traded by these companies is originating from FSC-certified forests. This CoC-certification is currently under review.
- Another controversial issue is the certification of timber and pulp [plantations](#). More than 7 million hectares of plantations and 30 million hectares of mixed forest have been certified to FSC standards. FSC recognizes that the implementation of the FSC Principles and Criteria for plantation management is open to a range of interpretations and has been controversial. As a result the scheme has embarked on a review of how it certifies plantations. The review is currently in its technical phase, operationalising the changes in the plantation policy approved in early 2007. FSC-members have agreed that FSC's experience with plantations must significantly improve to retain its credibility and to improve global management of plantations.⁷⁰

Protected areas and High Conservation Value Forests

Forestry activities in any of the protected areas covered by the [IUCN](#) I-IV categories, the [UNESCO World Heritage Convention](#) and the [Ramsar Convention](#) should be excluded from financing. This subject is dealt with in paragraph 4.1 on Biodiversity.

The concept of *High Conservation Value Forests (HCVFs)* was developed by the FSC to provide a framework for identifying forest areas with special attributes that make them particularly valuable for biodiversity and/or local people. In its origins, the concept was thus part of the FSC's overall framework aimed at improving forest management. The concept has since been more widely adopted, often without ensuring a link to crucial social and land use aspects that were ensured through the FSC's nine other principles and criteria.

The aim of applying this framework is to better identify and then design and implement appropriate management options for these areas in order to preserve or enhance their key ecological and socio-economic values.⁷¹ In some cases, effective protection of HCVF values will preclude expansion of industrial activities.

HCVFs are defined as "natural habitats where conservation values - including the presence of rare or endemic species, sacred sites, or resources harvested by local residents - are considered to be of outstanding significance or critical importance". The generic [Global HCVF Toolkit](#) provides guidance on how to apply the concept in specific situations. At present the toolkit is being revised to ensure that HCVF-assessments address the full range of values, take account of legality, customary rights and local consent requirements and are carried out in a participatory manner.⁷²

3.4.3 Content of a bank policy

By financing companies in the forestry sector, financial institutions can have a significant impact on forest conversion, degradation and destruction. A financial institution providing services to this sector must therefore develop a policy that sets conditions which should be met before providing financial services.

This policy needs to cover at least the forestry sector as such, comprising forestry, timber, pulp and paper, furniture and other wood-processing and trading companies. The following issues should be set as preconditions for financing in this sector:

- No forest conversion;
- No outstanding land use conflicts;
- FSC-certification for existing operations involved in managing forests and tree plantations;
- FSC *Chain of Custody* certification for their full supply chain for existing operations involved in trading and processing wood-products (including pulp, paper and plywood mills as well as furniture manufacturers);
- A clear and enforceable approach to achieve FSC-certification integrated in the project plan for all start-up operations in the forestry sector. This is especially important for plantations and pulp mills. These plans should be verified as follows:
 - For tree plantations an independent assessment of their environmental and social impacts is necessary, including the cumulative and macro impacts when new plantations are located in regions in which already many plantations are located;
 - For pulp mills an independent assessment has to verify the guaranteed availability of a sustainably produced supply of timber for the pulp mill.

Due to the ongoing revision of plantation certification within FSC, banks should not solely rely on the client's plans to achieve or maintain FSC certification of plantations. The social and environmental track record of the client should be checked as well and the environmental and social risks of doing businesses in countries with weak environmental law and/or implementation practices should be taken into account.

A bank can choose to integrate its forestry sector policy in a wider forest policy, which also covers all corporate clients in the agriculture, oil & gas, mining, dams and other industries which have impacts on forests. In this case the specifics of each sector should be dealt with in a sufficient way. Guidelines on how to deal with these sectors are provided in this and other paragraphs in this report. The [Guidelines for Investment in Operations that Impact Forests](#) which was published by WWF in September 2003 can also help banks identify critical issues and develop a forest policy.⁷³

If banks' policy would be wider than the forestry sector as such and would also cover other operations which can impact forests, the following preconditions for financing should at least be added to the policy:

- Commitment to identify and protect HCVMs in the forests managed by the client while ensuring local access and non-industrial use by local communities;
 - Identification of specified forest 'no-go zones' where industrial activities by clients will not be financed;
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- Specific acknowledgment of the rights to the fair and equitable use of forest resources by indigenous peoples and local communities;
- Commitment to further the goals of the FLEG processes in the client's sphere of influence.

Specific attention is needed for small-scale and community-based forestry operations, which are far more likely to operate in a sustainable way.

3.4.4 Scoring table

The considerations in the previous paragraphs lead to the following scoring table with regard to bank policies on forestry:

- 0. The bank has no policy on this sector;*
- 1. The bank's policy is vaguely worded or aspirational, with no clear commitments;*
- 2. The bank's policy excludes companies from financing that are directly or indirectly (as traders or processors) involved in corrupt practices, illegal logging, forest conversion activities which undermine the rights of local communities or operate in specified 'no-go zones';*
- 3. The bank's policy sets FSC-certification as pre-condition for clients operating in the forestry sector;*
- 4. The bank's policy sets FSC-certification as pre-condition for clients operating in the forestry sector and commits explicitly to the conditions mentioned in paragraph 3.4.3. Additionally, the bank has a clear preference to finance small-scale and community-based forestry operations, offering favourable financing conditions.*

3.4.5 Results

Eleven banks have developed and published a specific forestry policy, while another three banks have included lending criteria on forestry in other sector policies. HSBC (United Kingdom) has the best forestry policy, which also partly covers forest conversion, e.g. for the use of extractive industries. Some other banks also describe the effect of extractive industries on forestry, but set no strict requirements to their clients.

Scores on Forestry policies					
HSBC	3	Banco Bradesco	0	Nedbank	0
Bank of America	2	Banco Itaú	0	RBS	0
Citi	2	Bank Mandiri	0	Saudi-American Bank	0
Fortis	2	Bank of China	0	Santander	0
Goldman Sachs	2	BBVA	0	Scotiabank	0
ING	2	BNP Paribas	0	Société Générale	0
JPMorgan Chase	2	China Construction	0	Standard Bank	0
Merrill Lynch	2	Crédit Agricole	0	Standard Chartered	0
Royal Bank of Canada	2	Credit Suisse	0	State Bank of India	0
ABN Amro	1	Deutsche Bank	0	Sumitomo Mitsui	0
Banco do Brasil	1	ICBC	0	UBS	0
Barclays	1	Intesa Sanpaolo	0	Unicredit	0
Morgan Stanley	1	KBC	0	WestLB	0
Rabobank	1	Mitsubishi UFJ	0	Westpac	0
ANZ	0	Mizuho Financial	0	Dexia	X
