

Forest Land and Forest Products Sector Policy

Introduction

Forests cover four billion hectares, or 30%, of the world's land surface. They support a wide range of commercial activities, from logging operations to the manufacture of such products as plywood and paper. Other associated products such as palm oil or soy may originate from forest land which has been converted to plantations. The forest land and forest products sector plays a key role in world trade flows and, indeed, in world economic development.

Forests are also important because of their high biodiversity, which includes endangered species. They provide a home for forest-dwelling people, whose traditional lifestyles may depend on the forest. As a result, the sector's activities, if not managed responsibly, can have potentially significant impacts on both the environment and local communities.

HSBC has a long-standing commitment to sustainable development and, when supporting clients in the forestry sector, we seek to balance these complex economic, environmental and social issues. Our *Forest Land and Forest Products Sector Policy* provides guidance on sustainability standards applicable to our involvement in the sector. These standards represent international good practice and have been drawn up after extensive consultation with the industry and with other key expert stakeholders. The standards are consistent with our other policies, such as the Equator Principles framework which we apply to project finance activities. They also reflect HSBC's commitment to engage with the sector and to work with clients which are moving towards a sustainable business model. While not an easy strategy to implement, we consider engagement rather than exclusion as the right approach for a responsible bank to take.

This document is a summary of our policy. The principal elements are that it prohibits illegal logging and forestry in highly sensitive areas, and it supports clients whose operations are independently certified as legal and sustainable. A separate document on *Frequently Asked Questions* answers questions raised by stakeholders.

Scope

The financial services covered by the policy include all lending and other forms of financial assistance, debt and equity capital markets activities, project finance and advisory work.

The activities within the scope of the policy are: forestry and logging; timber processing such as sawmilling or the manufacture of panel products and wooden furniture; timber trading; the manufacture of pulp and paper; and plantations (timber, oil palm, soy and rubber).

Policy prohibitions

HSBC will not provide financial services which directly support:

- illegal logging;
- operations in UNESCO World Heritage Sites; and
- operations in wetlands on the Ramsar List.

Certification standard

HSBC requires clients to obtain independent certification, to our standard, that their timber operations and/or their supplies of timber products are legal and sustainable. Our standard is based on the

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Principles and Criteria of the Forest Stewardship Council (FSC) certification scheme and on our commitment to the Equator Principles, providing assurance as follows:

Legality. Logging and harvesting activities must respect permits; quotas; concession areas; local laws on taxation and corruption; protected species (including the Convention on International Trade in Endangered Species); the legal rights of communities; and areas defined as High Conservation Value Forest (HCVF)¹. We will not finance the conversion of HCVF to plantations and only consider low impact operations in HCVF.

Sustainability. As well as meeting the legality requirement, activities must minimise harm to ecosystems; maintain forest productivity; ensure forest ecosystem health and vitality; safeguard the traditional or customary rights of forest-dwelling communities (including protection of the rights of indigenous peoples, maintenance of community relations, benefits for local communities, protection of workers' rights and mechanisms for dispute resolution); and reflect a balanced participation of economic, environmental and social interests.

National and international certification schemes provide varying degrees of independent assurance on the legality and sustainability of activities in this sector. HSBC uses third party technical experts, aided by both publicly available and specially commissioned analysis, to determine the extent to which a scheme meets our standard. We approve, under our policy, certification schemes which meet our standard on sustainability and we note those which provide assurance on legality. The schemes are reviewed regularly and help us to determine whether our clients in this sector meet our policy. Clients are considered fully compliant with the policy when their activities are 70% certified as sustainable and there is evidence that the remainder is legal, in line with best practice certification procedures.

Certification may be neither a straightforward nor a quick process. Typically, clients follow a step-wise approach, either implementing certification progressively in different operations or providing assurance of legality before proceeding to sustainability. In line with our commitment to work with and encourage clients towards certification, we support these 'near-compliant' clients where they are on a credible path towards achieving compliance with our policy.

We consider five years as sufficient time for most clients to evidence material progress towards certification. HSBC's commitment to certified forestry was made in our original *Forest Land and Forest Products Sector Guideline* in 2004 and, therefore, we require clients to meet the standards of this policy by 2009. Where appropriate, the independent reviews required by our policy will also be required within this time-frame. For non-compliant clients who are making no progress towards compliance, we will take measures to exit such relationships.

Other policy restrictions and guidance

HSBC has a restricted appetite for other types of potentially high impact business and provides the following guidance:

HCVF. Where clients are not fully compliant with our policy and operate in countries with a high incidence of illegal logging, biodiversity or social conflict, independent confirmation will be required that their non-certified operations do not impact adversely on HCVF.

Plantations. HSBC will not finance plantations converted from natural forest since June 2004 (the date of our original *Guideline*) unless they are independently certified or confirmed as not having impacted adversely on HCVF. We do not support the clearance of forest land for plantations by burning.

Pulp and paper. HSBC will not finance the manufacture of pulp and paper where raw material supplies of wood are not certified in accordance with our policy.

¹ High Conservation Value Forest: forested areas containing biodiversity or other conservation values such as watersheds or cultural sites which are of outstanding significance or critical importance.

The policy also provides guidance on other sub-sectors with potentially high environmental and/or social impacts, including:

Biofuels. Demand for biofuels has increased significantly, driven partly by the belief that all biofuels are low carbon technologies and partly by the rise in their commercial viability. However, these factors need to be balanced by the fact that some biofuels are more carbon-intensive than others and by their potential impacts on HCVP, communities and food prices. We adopt a cautious approach to financing biofuels, ensuring that wider sustainability impacts are taken into account.

Palm oil and soy. We do not finance the conversion of HCVP for plantations and, in the case of palm oil, have a preference for clients who seek certification under the new Roundtable on Sustainable Palm Oil certification scheme. We actively support other multi-stakeholder initiatives to establish principles of sustainability for a wider range of agri-commodities.

Peat. We recognise that commercial activity in peatlands can have negative local impacts on biodiversity and communities, as well as wider impacts on climate change due to the significant levels of carbon dioxide captured in peat. We therefore take a cautious approach to business proposals in this sub-sector.

Best practice

HSBC will, where possible, support clients as they seek certification and move towards best practice on the management of sustainability impacts. As part of this approach, we have identified a number of organisations – or certification support providers – which can help clients with technical advice and guidance, including:

- Global Forest and Trade Network
- ProForest
- Rainforest Alliance
- Tropical Forest Trust

Summary

The forest land and forest products sector will remain a key sector in the world economy. It is important that the sector continues to demonstrate progress in successfully managing its potentially high sustainability impacts and, with increasing numbers of buyers seeking certified products, we believe that it is in the long-term interests of our clients to obtain certification. HSBC is committed to supporting clients who are independently certified as operating legally and sustainably. This policy sets out the terms of our engagement with the sector and the standards we expect our clients to achieve. The policy also provides practical tools to assist our work with clients and to implement the policy. In this way, the *Forest Land and Forest Products Sector Policy* reinforces HSBC's commitment to sustainable development and the attainment of a balance between economic, environmental and social factors.