

Forest Project Analysis
International Methods & Ethical
Standards

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EMRG INC/Forest Trends

Background Cary Raditz

- 35 years working in developing economies
- International banker (Chemical Bank NY)
- CFA--Chartered Financial Analyst®
- Speaker: CFA Institute
- Specialty Finance practice manager Barents Group/KPMG
- Trained Bankers at ICBC Beijing in 2000
- Consulting to *Forest Trends*: ITTO study

Outline of Presentation

- Due diligence
- Investment industry ethical standards
- Environmental banking standards
- Implications to the lending and investment decision process
- Action taken by international banks

Loan and Investment Screening

- For credit due diligence
- Size and location of forestry operation
- Experience of management
- Audited financial statements
- Certified or non-certified
- Transparency and disclosure--accounting policies, wood tracking systems

Global Investment Standards

Bond rating company guidelines

General investment analysis practices

Investment management firm standards

--CFA Institute® www.cfainstitute.org

--CFA® Chartered Financial Analyst program

Best Practice Ethical Guidelines

- CFA Institute Code of Ethics, Standards of Professional Conduct, Code of Ethics, Global Investment Performance Standards
- AIMR and National Investor Relations Institute jointly proposed ethical guidelines in March 2004
- Respond to recent corporate scandals

...Market scandals

- United States scandals: Enron, WorldCom
- ... Asian forestry stock collapses 95% in less than a decade
- ...lack of transparency, disclosure, exceeding environmental expectations
- ...on going problems of APP, Gunns, shareholder advocacy, restricted markets

...Corruption

- Forestry has been a wild frontier
- Corruption attracts the unscrupulous, repels long term investors
- Investors measure corruption
- Corruption index: Transparency Intern'l
- <http://www.transparency.org/cpi/index.html#cpi>

	Country rank	Country	CPI 2003 score	Surveys used	High-low range
<p>Low</p>  <p>High</p>	1	Finland	9.7	8	9.2 - 10.0
	18	USA	7.5	13	4.9 - 9.2
	37	Malaysia	5.2	13	3.6 - 8.0
	54	Brazil	3.9	12	3.3 - 4.7
	59	Peru	3.7	9	2.7 - 4.9
	64	Mexico	3.6	12	2.4 - 4.9
	66	China	3.4	13	2.0 - 5.5
	70	Thailand	3.3	13	1.4 - 4.4
	86	Russia	2.7	16	1.4 - 4.9
	100	Vietnam	2.4	8	1.4 - 3.6
	113	Congo, Republic	2.2	3	2.0 - 2.8
	118	Papua New Guinea	2.1	3	1.5 - 2.7
	122	Indonesia	1.9	13	0.7 - 2.9
	124	Cameroon	1.8	5	1.4 - 2.0

Environmental Issues

- Can environmental factors be a liability to a bank or investor group?
- Will international banks restrict lending to projects violating environmental standards?
- Tropical forestry is controversial
- Are certification, FSC “best practices”
- IFC and Equator Principles are benchmark ethical standards

Equator Principles

1. Based on IFC screening procedures
 2. Borrowers make Environmental Assessment
 3. Environmental, Health and Safety Guidelines for all countries
 4. 10 major Safeguard Policies for low and middle income countries
 5. Borrowers consult with local stakeholders.
- Source: *www.ifc.org/equatorprinciples*

Banks Endorse Equator Principles

- 23 international banks including Citibank, HSBC, ABN AMRO, Barclays, Credit Lyonnais, Credit Suisse Group,
- Did \$14.5bn in project finance in 2002
- 30% of global project finance syndications
- Next step– bank implement internal environmental policies

Internal Bank Forestry Policies

- Internal forestry policies at Citibank, HSBC and other first tier banks
- Consistent approaches in categorizing projects
- Categories: high, medium and low environmental and social risk
- Banks will require their customers to demonstrate compliance with IFC safeguard policies and World Bank

Benefits to Banks

- Better manage the credit risk and reputation risk
- Customers must demonstrate compliance
- Principles have real teeth: loan covenants
- Banks can declare non-compliant loans in default.

Example, Citibank Policies

- Part of Citigroup's overall Global Corporate and Investment Banking (GCIB) Group Environmental and Social Risk Management Policy
- An internal anti-illegal logging task force
- Revising credit procedures
- Challenges in implementation of policy

Project warning signals

- Foggy or transparent accounting practices
- Operations show unsustainable practices
- Poor cash flows, high leverage (market is cyclical)
- Forest management plans? Certified?
- Log tracking systems, chain of custody
- Environmental and social plans
- Controversy? Corruption? Scandal?

Summary

- Due diligence is important in project analysis
- Importance of transparency, compliance to legal, regulatory and environmental standards
- Shareholder perception of the environment gains importance
- Top tier international banks are implementing internal environmental policies
- Chinese banks and investment companies should endorse Equator Principles and set up internal policies

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