

# Asia Pulp and Paper

Risk briefing for banks and investors



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## Summary

The Indonesian pulp and paper giant Asia Pulp and Paper (APP)<sup>1</sup> is controlled by the Sinar Mas Group, one of the largest conglomerates in the country. APP has a thirty-year track record of negative social and environmental impacts across its supply chains. The company over many years has been associated with deforestation, massive greenhouse gases emissions, forest fires, land conflicts and displacement of communities, violence and even killing of environmental activists; issues that are in clear dissonance with the company's own commitments, as well as government regulations and laws, such as those on peatland and haze protection.

Despite its commitments, APP's harmful practices continue, and the company is further expanding its operations in ways that will have catastrophic consequences for forests, peatlands and communities, as with the planned expansion of the OKI mill.

APP's operations represent major risks for banks and investors. This risk briefing sets the reputational, financial, regulatory, legal, and other risks to banks and other financial institutions that consider exposing themselves to the company and its abuses.

### Summary of major risks for banks and investors

**Stranded asset risks:** The concept of 'stranded assets' is well-known in relation to climate risk, and the same logic applies to the unsustainable production of forest-risk commodities.<sup>2</sup> For example, action by the Indonesian government to stop deforestation and retire plantations from peatland could pose a risk to current and undeveloped plantations.

**Future cost of social conflicts:** Unresolved social conflicts risk further liabilities for APP. We projected the potential costs of unresolved social conflicts at APP supplier plantations at between US\$ 0.7 and 5.7 billion (see below).

**Market risks:** APP's failure to comply with a "No Deforestation, No Peat, and No Exploitation" (NDPE) standard, exacerbated by the need to find wood-fibre to feed its expansion plans, risks leaving the company excluded by buyers with NDPE policies in place covering their pulp and paper supply chains.

**Regulatory risks, legal and compliance risks:** Fires stemming from concessions on dried peat have led to four ongoing legal investigations into APP suppliers from Singapore, and further fires are likely to trigger additional transboundary procedures.

**Fibre supply risk:** APP disclosed sources for 15.7 million cubic metres of wood, covering only around half of the fibre the plant will need to produce to its designated capacity.<sup>3</sup> Future constraints in the company's ability to use the existing plantation area may arise due to regulation or flooding caused by peat subsidence, risking worsening the situation.

**Reputational risks:** Repeated broken promises and continuous human rights abuses and environmental impacts have demonstrated APP's inability to meet its own commitments as well as assure investors they will not be exposed to risks from APP's environmental and social harms. On the contrary, APP's need to expand its plantation bank to feed the OKI mill will further expose investors and business partners to reputational risk.

*We wrote to APP, giving them the opportunity to respond to questions regarding its planned expansion of its OKI pulp and paper mill. We were pleased to see that APP provided a response, of which relevant parts can be found in the ["Appendix: Asia Pulp & Paper response"](#) on page 10.*

## APP's past and present impacts

Major social and environmental impacts connected with APP's operations have been widely documented by a number of local and international organisations.<sup>4</sup> Already in 2013, APP adopted a Forest Conservation Policy in which it committed to end deforestation in its Indonesian concessions.<sup>5</sup> However, despite this and previous commitments, the company continues to source fibre from deforested areas, degrade precious peatlands and fuel social conflicts.

### Deforestation and forest degradation

A 2010 report by Eyes on the Forest estimated that APP has been responsible for deforestation of an area of more than two million hectares in the provinces of Riau and in Jambi, Indonesia between 1984 and 2010.<sup>6</sup> Despite APP's 2013 Forest Conservation Policy, the deforestation has continued since, albeit at lower rates. A 2018 Greenpeace study revealed that from 2013 to 2018, almost 8,000 hectares of forest and peatland were cleared in two concessions linked to APP and its parent company Sinar Mas Group.<sup>7</sup> A second Greenpeace study found that between August 2018 and June 2020, around 3,500 hectares of peatland were destroyed in three concessions either owned or that are major suppliers to APP.<sup>8</sup> While land clearing by APP fibre suppliers decreased after its 2013 commitment, the destruction of peatland by fires increased.<sup>9</sup>

### Forest and peatland fires

Most APP fibre supply plantations lie on dried peat soil, which is highly flammable, a major factor causing large-scale fires and releasing large amounts of carbon emissions. The resulting haze crises have a tremendous impact on public health, and it is feared that the impact of another haze crisis will even be worse due to the additional effects of the COVID pandemic on affected populations.<sup>10</sup>

By choosing to operate in this highly sensitive peatland ecosystem, APP greatly increases fire risks, as plantations on drained peat are highly susceptible to catching fire and constitute a large store of fuel that is impossible to control once fires start.

### APP, peat, fire & haze:

Extensive plantations on dried peat are a major factor causing large-scale fires, especially in combination with extreme dry weather seasons caused by climate change. The years 2015, 2017 and 2019 saw the most intense burning of forests in Indonesia's history,<sup>11</sup> creating a smoke and haze crisis that affected all Southeast Asia. The 2015 fires in Indonesia burned 2.6 million hectares<sup>12</sup> of forest, peat and other land, releasing 1.75 billion tonnes of carbon dioxide was released in just a few months.<sup>13</sup> It was estimated that the 2015 fires could cause more than 100,000 premature deaths in the region.<sup>14</sup> A large part of the fires in South Sumatra happened in APP concessions: in 2015, the total area of forest burned inside APP concessions in South Sumatra province was 293,065 hectares, nearly three-fifths of which constituted carbon-dense peatland.<sup>15</sup> In 2019, APP concessions in South Sumatra burned again; they were among the worst burned areas in Indonesia, with a total affected area of more than 60,000 hectares.<sup>16</sup> In the same year, Sinar Mas' pulpwood concessions and those of its suppliers had the largest burned area of any corporate group.<sup>17</sup>



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## Greenhouse gas emissions

Swamp forests which have been drained for plantations can release up to 80 tonnes of CO<sub>2</sub> per hectare into the atmosphere every year. Furthermore, peat fires (see above) cause additional greenhouse gas emissions.<sup>18</sup> Indonesia accounts for 36% of global carbon rich peatlands, and nearly 680,000 ha - or about 55% - of the planted area supplying APP is on peatlands, leading to massive greenhouse gas emissions.<sup>19</sup> Recently, NGOs estimated that, without taking into account forest fires and downstream emissions, APP's wood suppliers released approximately 430 million tons of CO<sub>2</sub> equivalent (CO<sub>2</sub>e) over the period 2015-2019; an average of 86 million tons CO<sub>2</sub>e per year, more than Singapore's total annual emissions.<sup>20</sup> While APP claims to have plans to achieve a 30% reduction in its carbon footprint<sup>21</sup>, APP's plans don't include reduction of the company's main source of emissions: land use and land use change across its wood fibre supply chain.

## Social conflicts

Despite APP's commitment in its Forest Conservation Policy to respect the Free, Prior, and Informed Consent (FPIC) of Indigenous Peoples and local communities, hundreds of social conflicts and land disputes take place in APP concessions. An investigation by the Environmental Paper Network that mapped social conflicts in pulp-wood plantations in Indonesia revealed that in five provinces (Riau, Jambi and South Sumatra, West Kalimantan and East Kalimantan), at least 107 villages or communities are in active and ongoing conflict with APP affiliates or its suppliers. In addition, the study identified 544 villages or communities with potential for further conflicts, located inside or adjacent to concessions of APP's suppliers, covering an area of roughly 2.5 million hectares.<sup>22</sup> APP suppliers have been linked with several incidences of violence in recent years. In 2015, security contractors for one supplier killed a farmer activist, and in 2020 another APP supplier sprayed herbicide by drone on food crops grown on disputed land during the Covid pandemic.<sup>23</sup> In 2021, another APP supplier was responsible for assaults on Indigenous women protecting their ancestral land.<sup>24</sup>

# Risky expansion plans: the OKI mill and the Domtar acquisition deal

## OKI Mill expansion

APP operates one of the world's biggest pulp mills, the *Ogan Komering Ilir (OKI)* mill in South Sumatra, and has plans to **triple** its production from 2.45 millions to 7 millions tons of kraft pulp.<sup>25</sup> This expansion will increase the mill's dependency on high-carbon peatlands for fibre supply - yet the company has not presented a credible sourcing or wood supply plan. The Environmental Impact Assessment for the OKI mill indicates that 30.1 million tons of wood is required for 7 million tons of pulp capacity.<sup>26</sup> It also indicates sources for 15.7 million cubic metres of wood, which is roughly half the 30.1 million tons of wood required. However, the expected sources for the other half are unknown, and APP's lack of transparency over its long-term wood supply plan should be a cause for significant concern, including for banks and investors.

The OKI mill environmental impact analysis (AMDAL) considers environmental risks related to waste management, but not the environmental impacts of wood suppliers, such as impacts from peat drainage and eventual plantation expansion in natural forests due to the increased need for wood fibre. It also categorises the fire risk as a "natural disaster", misleading potential investors.

APP's expansion of the OKI mill will also lead to increased greenhouse gases emissions, as the emissions from land use/land use change (including fires) across APP's wood fibre supply chain is the largest source of emissions in APP's business. OKI's expansion will also threaten efforts to control fires, social conflicts and deforestation in Sumatra and Kalimantan. The top three suppliers to the OKI mill are located in some of the worst burned areas in Indonesia's 2015 and 2019 fires.<sup>27</sup>

## Questions for APP

- Has APP undertaken a comprehensive GHG inventory for its entire business including emissions from land-use/land-use change across its wood fiber supply chain? If so, please make these estimates publicly available.
- Can you confirm that GHG emissions from land-use/land-use change (including fires) across APP's wood fiber supply chain are the largest source of GHG emissions in APP's business?
- It is estimated that nearly 680,000 ha, or 55% of the planted area supplying APP is on peatlands. Of APP suppliers' overall concession area of 2.6 million hectares, 790,000 ha of peatlands (30% of the total concession area) were designated as 'protected' under the 2016 Peatland Regulation by [the Ministry of Environment and Forests] 'KLHK'. How much wood production area did APP estimate it would lose if the 2016 regulation to protect and restore peatlands was fully implemented?
- The Environmental Impact Assessment (Amdal) for the OKI mill expansion indicates that 30.1 million tons of wood are required for 7 million tons of pulp capacity. The Amdal also indicates sources for 15,725,540 m<sup>3</sup> of wood, which is roughly half the 30.1 million tons wood requirements. What are the expected sources for the other half of the wood requirement?
- Has APP estimated the amount of fine particulate matter below 2.5 microns (PM<sub>2.5</sub>) released from APP suppliers areas that burned in 2015 and 2019? If APP has made these calculations/estimates, please share them with us.

## Domtar acquisition

In July 2021, Barclays, Credit Suisse and Bank of Montreal committed to a total of US\$ 1.95 billion of financing to support APP's affiliated company Paper Excellence in its acquisition of Canadian pulp & paper company Domtar.<sup>28</sup> Paper Excellence is a relatively unknown company, part of the Widjaja conglomerate, that recently built a global empire by acquiring pulp and paper mills in Canada, Europe, and Brazil.

As a result of the transaction, Domtar and Paper Excellence risk losing their Forest Stewardship Council (FSC) certification, as FSC has already disassociated itself from APP<sup>29</sup>, meaning that no products from the group can be certified by FSC.

## Risks for banks and investors financing APP and related companies

Financial links with the Sinar Mas Group, APP, and its subsidiaries represent a range of risks for banks and investors.

**Stranded assets:** There is a substantial risk that concessions for pulp plantations in Indonesia may turn into stranded assets in the near future. The Indonesian government has stepped up efforts to reduce greenhouse emissions, resulting in stricter sustainability commitments that could pose a risk to existing (and to be developed) plantations. A recent report analysed stranded asset risk for the palm oil sector in Indonesia and found more than two-thirds of unplanted concessions could be stranded by 2040.<sup>30</sup> Similar risks are likely in the pulp and paper sector, which is increasingly under pressure to ramp up action on climate. Furthermore, peat soil subsidence due peat erosion will put large parts of existing plantations out of business due to flooding (see below).

**Costs of social conflicts:** Ongoing and unresolved social conflicts in APP wood supplier plantations create risks for further financial liabilities for the company. The social compensation risk due to social conflicts at APP supplier plantations is projected to be between USD 0.7 and 5.7 billion.<sup>31</sup> This figure refers only to conflicts that are known by local civil society organisations; the actual number of conflicts may be much higher.<sup>32</sup>

**Market risks:** APP's failure to comply with certain standards from buyers - such as NDPE policies that cover the pulp and paper sector - can lead to cancelled contracts and a decrease in demand. Moreover the acquisition of Domtar could pose a market risk as the company risks losing its Forest Stewardship Council (FSC) certification.

**Legal and compliance risks:** APP's expansion plans can lead to transboundary legal investigations with neighbouring countries affected by the haze, as has already occurred with the four investigations into APP pulpwood suppliers under way in Singapore under the Transboundary Haze Pollution Action (THPA).<sup>33</sup> Indonesian governmental regulations indicate that in order to prevent fires, peat must be protected and restored.<sup>34</sup> APP already had problems of legal compliance on this, and is likely to have more in the future due to its expansion plans.<sup>35</sup>

**Fibre supply risk:** APP's failure to set out full sourcing plans for its OKI mill poses major supply and operational risks. Social conflicts and peat fires pose further threats as large areas of plantation may be affected by social unrest and by regulations aimed to control fires.

Furthermore, the wood fibre sources already secured are at risk too. When dried peat releases its carbon into the atmosphere, it dissolves, leading the peat soil to subside and become prone to flooding. This represents a long-term risk to APP's wood fibre supply. A 2015 study by Delatares stated that drained plantations on peatland cannot be sustained, ultimately making them economically unviable and resulting in abandonment.<sup>36</sup>

**Reputational risks:** Repeated broken promises and continuous human rights abuses and environmental impacts have demonstrated APP's inability to meet its own commitments.<sup>37</sup>

APP's expansion plans risk massive deforestation, increased CO2 emissions, and more forest fires, which also put regional health at further risk. Financial institutions supporting APP, including via Domtar, Paper Excellence and affiliated companies, are exposing themselves to serious reputational risks as a result of these impacts. The reputational risk for business partners is exacerbated by the untransparent corporate structure.

## Lack of transparency

APP is part of a nebula of companies linked by a deliberately complex and opaque corporate structure comprising the Sinar Mas Group. Many companies of the Sinar Mas Group are incorporated in tax haven countries, hindering transparency. This ownership structure is often used to shield the parent company from legal liability. It facilitates the impunity of APP, and all affiliated companies, and it makes it harder to hold any company accountable for its massive environmental and social abuses.<sup>38</sup>

Some of the companies in this structure are formally part of the Sinar Mas conglomerate, while others are formally independent but still controlled by the Widjaja family, operating with a single commercial strategy.<sup>39</sup> Several of the corporate associations of these companies are likely purposely kept hidden, possibly for commercial or fiscal reasons, but probably also to deny links with deforestation or so that parts of the company can keep using FSC certification despite the wider APP group being “dissociated” by FSC.



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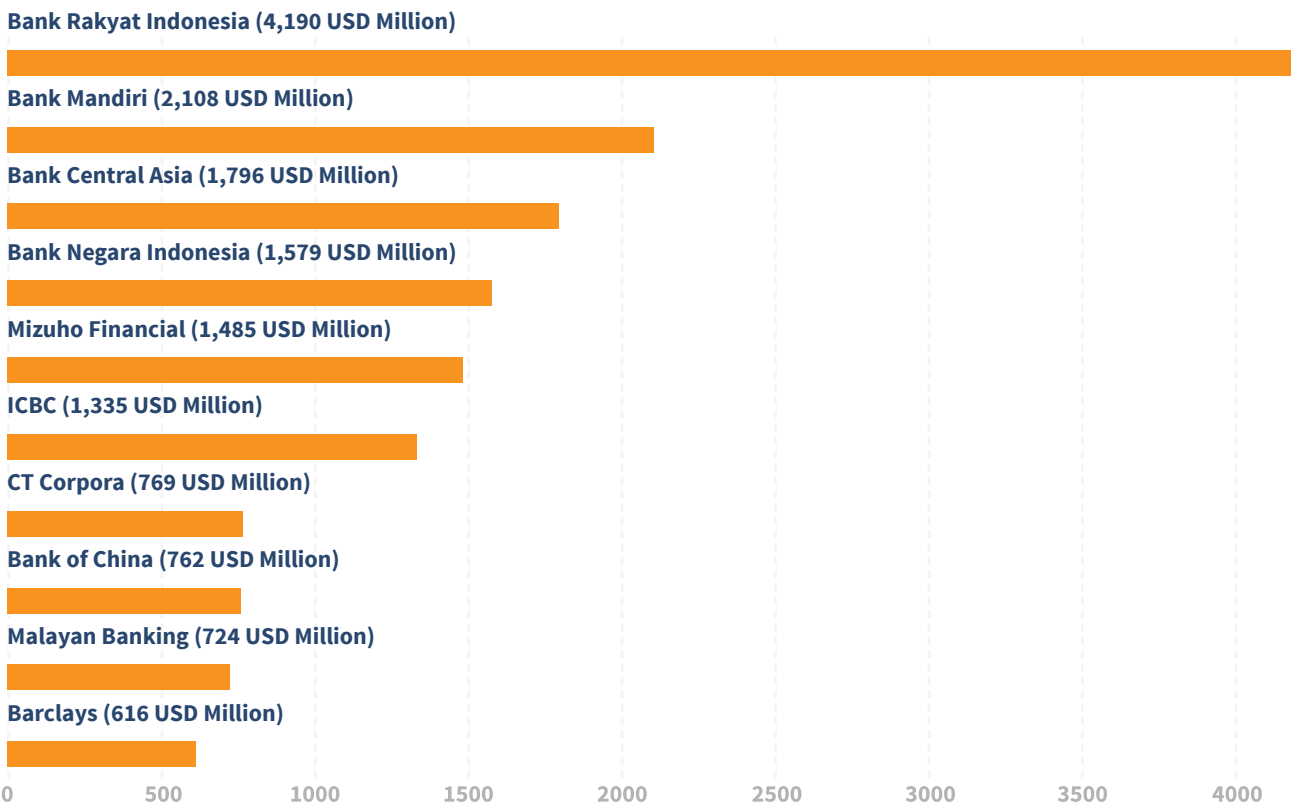
## Financiers exposed to APP's risky business

According to data from the Forests & Finance database, the top three financiers of pulp and paper concessions owned by APP and other subsidiaries of the Sinar Mas Group are the largest Indonesian banks. Bank Rakyat Indonesia is the largest creditor, having provided USD 3,906 million in finance to Sinar Mas pulp and paper concessions between 2015 and 2021. Bank Central Asia and Bank Mandiri follow, with credit exposure amounting to US\$ 1,701 million and US\$ 1,978 million respectively for the same period. Other financial institutions with significant exposure to the group include North American and European asset management firms, such as Vanguard, BlackRock and Dimensional Fund Advisors.<sup>40</sup>

Furthermore, Barclays, Credit Suisse and Bank of Montreal are exposed to APP and the Sinar Mas Group through their recent financial support for APP-linked Paper Excellence's acquisition of Domtar.<sup>41</sup> This presents conflicts with these banks' commitments as signatories of the Principles for Responsible Banking and their own sector policies.

### Top creditors of Sinar Mas' pulp and paper concessions

Source: Forests & Finance database





## Conclusion

Financing APP continues to be a risky business. After decades of abuses, the company lost any credibility in meeting its own commitments. Banks should therefore consider all the risks associated with the group, and are recommended to **halt any current financing and refrain from any future financing for APP, Sinar Mas Group and affiliated companies** until the conglomerate can prove and verify that it has made radical changes across its business and eliminated all forms of deforestation, peatland destruction and human rights abuses from its supply chains. Likewise, investors and other financial institutions with exposure to APP, Sinar Mas Group and/or its affiliated companies should be aware of the material financial risks, divest of any investments and consider future potential risks in engaging with the conglomerate.

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## Contact

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## Appendix: Asia Pulp & Paper response

We wrote to APP, giving them the opportunity to respond to questions regarding its planned expansion of its OKI pulp and paper mill. We were pleased to see that APP provided a response, relevant sections of which can be found below”

- **Overall:** APP stated that many of these issues are “regularly disclosed in our annual [Sustainability Report](#)” and that “APP remains firmly committed to its [2013 Forest Conservation Policy](#). All new and existing suppliers, regardless of ownership, must comply with these policies, and be in alignment with our Sustainability Vision”.
- **Covering peatlands:** APP stated that “Protected peatlands are an integral part of our ecosystem, which is why APP has conducted detailed LiDAR exploration of supplier concessions to better understand and locate critical peatland areas. Not only that the LiDAR was able to map out all peat and non-peat area, allowing us to determine the type of land we operate on. Following which we submitted our updated maps to the Government based on field surveys and complete verification in 2018. In fact, prior to APP receiving the HTI license for OKI, the production was identified as non-peat as the area was experience huge fires twice in the early 90s.”
- **On Social Conflicts:** APP’s stated position on Social and Land Conflict is published [here](#).
- **Covering the OKI expansion:** APP states that the environmental impact assessment “AMDAL [for OKI] is still in revision and is yet to be submitted for approval. If expansion of the operational plantation area is required, this will be done responsibly, maintaining zero forest conversion, and in collaboration with local communities through the FPIC process.”
- Regarding APP’s ability to **source sustainable plantation wood fibre**, APP stated that: “We have invested heavily into the research and development of fiber crops and are continually seeing improvement in mean annual increment (MAI) per productive hectare. Through this we identified that using the existing plantation area, we could potentially double our plantation production just by utilizing it effectively. Any additional wood supply through partnerships with responsible producers, locally, in the region, or even further away with must comply with APP’s FCP and the SERA process.”

## Endnotes

- 1 See BankTrack's Dodgy Deal profile on APP [here](#).
- 2 CDP, "[From Risks to Revenue](#)", 2017
- 3 Environmental Impact Assessment (AMDAL) for the OKI mill expansion.
- 4 For detailed information about the impacts of APP operations, please check the Environmental Paper Network reports [Sustainability Default](#) and [Conflict Plantations](#) and Greenpeace's article "[This company promised to stop deforestation. But we caught them out.](#)"
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- 25 See [open letter concerning threats from the proposed expansion of the PT. OKI pulp and paper mill - APP Sinar Mas](#), 2021.
- 26 Eco Business, [Revealed: APP's controversial Indonesian paper mill OKI plans to triple size](#), 2021.
- 27 [Open letter concerning threats from the proposed expansion of the PT. OKI mill pulp and paper mill - APP Sinar Mas](#), 2021.
- 28 Business Wire, [Paper Excellence received finance \\$ 1.95 billion of financing commitments and reaffirms Domtar closing date](#), 2021.
- 29 FSC case information on APP, please see [here](#).
- 30 Orbitas, [Agriculture in the Age of Climate Transitions](#), 2021.
- 31 Environmental Paper Network, [Defaulting Social Conflict Resolution](#), 2020.
- 32 Environmental Paper Network, [Conflict Plantations](#), 2020.
- 33 Parliament Singapore, [Efforts made to investigate open cases against four companies under Transboundary Haze Pollution Act in 2015](#), 2020.
- 34 See Regulation 71/2014 on Peatland Protection, Law 32/2009 on Environmental Protection and Management, Law 4/1982 on Environment and Presidential Decree 32/1990 on Protected Areas Management.
- 35 See for examples: <https://foresthints.news/csos-backgovts-law-enforcement-efforts-against-apps-peat-violations/>; <https://www.wetlands.org/publications/will-asia-pulp-paper-default-on-its-zero-deforestation-commitment/>; and <https://news.mongabay.com/2016/12/as-accusations-fly-paper-giant-appears-to-stand-by-its-replanting-of-burned-peat-in-sumatra/>.
- 36 Deltares, [Assessment of impacts of plantation drainage on the Kampar Peninsula peatland, Riau](#), 2015.
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