

# SUSTAINABILITY STANDARDS IN CHINA–LATIN AMERICA TRADE AND INVESTMENT

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A discussion

EMMA BLACKMORE, DANNING LI, SARA CASALLAS – 2013



SHAPING  
SUSTAINABLE  
MARKETS

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For further information please contact: International Institute for Environment and Development (IIED), 80–86 Gray's Inn Road, London WC1X 8NH, United Kingdom. [newbooks@iied.org](mailto:newbooks@iied.org), [www.iied.org/pubs](http://www.iied.org/pubs)

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#### About the authors

Emma Blackmore is a researcher in the Sustainable Markets Group at IIED. She manages IIED's Shaping Sustainable Markets initiative, which explores the use and impact of market governance mechanisms. Emma has carried out research on how sustainability certification can benefit the poor, with a focus on Asia, carbon emission labels, contract farming, integrating small-scale farmers into global value chains and China's overseas investment. She is particularly interested in China's present and future engagement with sustainability standards, both international and national, and the impacts these standards will have on the millions of small-scale producers that drive many of China's industries.

Danning Li studied economics at Tsinghua University in Beijing and subsequently worked for Accenture Consulting for almost five years. In 2011, she worked for The Nature Conservancy, China, on a land trust project in one of the important giant panda habitats in Sichuan. The project established the first privately-owned nature reserve in China. More recently, Danning obtained an MSc in Environment and Development at the King's College, London. For her thesis, Danning studied the notions of nature in China and their implications for ecotourism. Danning is currently working for The Nature Conservancy,

Europe, to develop their work on international government relations from the Chinese perspective. One goal of this work is to facilitate environmentally sustainable investment and trade of Chinese companies overseas.

Sara Casallas currently works as the assistant for the Americas at the Ramsar Convention on Wetlands. She provides technical support for the region in order to implement the convention and promote the wise use of wetlands and of natural resources in general. Sara has previously held various research assistant and intern positions that focused on natural resource management and sustainability issues in the private sector. Before Ramsar, Sara was an intern at IIED's Sustainable Markets Group and collaborated on the research for this discussion paper while finishing her MSc in Global Environmental Change at King's College London. Sara is particularly interested in natural resource management and environmental legislation in the Americas region with a special focus on the neotropics.



# ACRONYMS AND ABBREVIATIONS

CBRC	China Banking Regulatory Commission
CDB	China Development Bank
Cerflor	Certificação Florestal (Forest Certification, Brazil)
CERTFOR	Sistema Chileno de Certificación de Manejo Forestal Sustentable (Sustainable forestry certification Chile)
CFCC	China's Forest Certification Council
China EXIM bank	China Export and Import bank
CNFPIA	China's National Forest Products Industry Association
CoC	chain of custody
EIA	Environmental Impact Assessment
EITI	Extractive Industries Transparency Initiative
Fedefruta	National Federation of Fruit Producers of Chile
FDI	foreign direct investment
FSC	Forest Stewardship Council
GRI	Global Reporting Initiative
ICMM	International Council for Mining and Metals
IUCN	International Union for Conservation of Nature
MEP	Ministry of Environmental Protection (China)
MOFCOM	Ministry of Commerce (China)
PEFC	Programme for the Endorsement of Forest Certification
RSPO	Roundtable on Sustainable Palm Oil
RTRS	Round Table on Responsible Soy
SFA	State Forestry Administration (China)
SFM	sustainable forest management
SME	small or medium-sized enterprise
SOE	state-owned enterprise
TNC	Nature Conservancy
ZTFC	Zhonglin Tianhe Beijing Forest Certification Center



# SUSTAINABILITY STANDARDS IN CHINA–LATIN AMERICA TRADE AND INVESTMENT

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# ONE INTRODUCTION

Trade and investment flows are increasing between emerging and developing countries. China in particular is becoming a growing force in global investment and trade with developing countries. This trade and investment offers opportunities to finance long-term development in countries where capital is scarce, and for innovation 'under the frame of South–South cooperation and globalization' (Ren, 2011). The new players and potential scale of this trade and investment bring new challenges and opportunities for sustainability.

'Sustainability' standards and codes, both public and private, are one way to govern this trade and investment, and to enhance its contribution to positive social and environmental outcomes. But the traditional focus of sustainability initiatives and mechanisms to date has been on the trade between developed and developing countries, rather than between emerging and developing countries. Indeed, there are a large number of private standards, beyond domestic legislation, governing this trade and investment to drive sustainability, especially in the natural resource and extractive industries. Well-known examples include the International Finance Corporation's Performance Standards, the Equator Principles, the OECD Guidelines for Multinational Enterprises, the Principles for Responsible Investment, the Extractive Industries Transparency Initiative (EITI), the Round Table on Responsible Soy and Roundtable for Sustainable Palm Oil, (RTRS and RSPO), Forest Stewardship Council (FSC), GlobalGAP and Fairtrade.

However, these standards are not necessarily appropriate for trade between emerging and developing economies. They do not always suit the different economic, socio-political, environmental and business contexts in which they may be applied, and may therefore lack local legitimacy. There are also fears that these mechanisms could act as barriers to trade. Many of these 'international' codes and standards have often been developed without the (meaningful) participation of relevant stakeholders in these countries, despite employing multi-stakeholder processes.

New types of players – such as Chinese state-owned enterprises, which are now sizeable investors in other emerging economies – present new challenges (and opportunities) for the application of private voluntary standards. These standards have been traditionally applied to and implemented by private enterprises. And while engaging with state-owned enterprises in sustainability efforts is important, there is also a vital need to be sensitive to the needs and challenges faced by small and medium-sized enterprises (SMEs) in working towards sustainability. When designing and implementing sustainability standards in these new contexts, it will be important to avoid potential unintended consequences, such as the exclusion of smaller players and the exacerbation of inequality which has resulted from the design and implementation of standards in trade between developed and developing countries (Blackmore and Keeley, 2012).

There is a need to engage with developing- and emerging-economy players in collective sustainability efforts and to improve understanding of current efforts towards sustainability in trade and investment, the drivers of these efforts, and their impact. What might the international community learn from these efforts and what might the experiences of developed/ developing-country trade offer in terms of lessons on the effective use and design of sustainability standards?

The following questions are relevant but at present there is insufficient knowledge to answer them appropriately:

- To what degree are 'international' sustainability standards being used by players in developing and emerging economies, and under what conditions? And why are these being used?
- What 'local' mechanisms are being used instead of, or in addition to, these standards – and are they harmonised against international codes and standards? To what extent are these local mechanisms being applied to trade between emerging and/or developing countries?
- What is the role of China, in particular, as the world's fastest-growing economy, in driving the development and use of standards, particularly in its trade with emerging economies?
- In light of the dominant role of Chinese state-owned enterprises in investments in other emerging and developing countries, what standards are being developed to shape their behaviour?
- What impact are these standards having, particularly in terms of excluding or including smaller players?

This discussion paper explores initial trends in mining, agriculture and forestry in trade and investment between China and Latin American countries, focusing on the implementation of sustainability standards. We also explore some of the public standards and guidelines being developed in China to shape its overseas investment. This paper is based on preliminary research, to serve as a starting point for further discussion and research. We focus on three Latin American countries – Chile, Peru and Brazil – recognising that they have differing regulatory regimes. These countries were selected because of their sizeable trade with China. The paper also focuses heavily on China's role *in* these countries (rather than the role of Latin American countries in China). This reflects the dominant direction of trade and investment at present.

This paper is based on an initial review of the existing, although sparse, literature, as well as a number of interviews with employees of select companies based in China and Latin America, industry associations, local NGO workers, government representatives and academics working in related fields (see Appendix 1). It concludes by identifying a number of further research questions, particularly around the effectiveness of tools currently being used and developed and the need to consider the role for SMEs in the development and use of sustainability standards.

# TWO

# GROWING TRADE AND INVESTMENT BETWEEN CHINA AND LATIN AMERICA

Much attention, particularly in the media, has been paid to the growing role of China in Africa – for example over 'land grabs' and whether China's presence will bring benefits or costs for Africa, and its wider implications for the global aid paradigm (see Buckley, 2012). Seemingly less attention has been paid to China's growing role in Latin America, despite it being the second biggest recipient of Chinese investment (after Asia) (Ren, 2011).

Indeed, trade and investment between China and Latin America has increased at unprecedented rates in the past six years. In 2006, exports from Latin America and the Caribbean to China had reached a value of US\$22.6 billion. By 2010, the corresponding value had increased to almost US\$72 billion – an annual growth rate of almost 34 per cent (ECLAC, 2011b). At a regional level, China is Latin America's third biggest trade partner and is expected to be its second biggest trade partner by 2014 (ECLAC, 2011a).

This trend is expected to continue, driven by the increase in China's demand for raw materials and a search for markets that have been less affected

in the economic crisis. China is now a major buyer in the natural-resource-based commodity sectors of mining, agriculture and forestry, predominantly in Brazil, Chile, Peru and Argentina. China's 'going global' strategy<sup>1</sup> is explicitly encouraging Chinese companies to invest overseas and to increase cooperation with other emerging economies. China is seeking to increase its 'soft power' and build positive diplomatic relations with other countries – increasing investment and strengthening trade ties with particular countries, while not undermining other states' sovereignty.

The Chinese government has adopted diplomatic and trade measures with Latin America to drive economic growth and development, guarantee long-term supply of raw materials and enhance its soft power. These measures include different types of foreign direct investment (FDI) as well as donations, long-term purchasing contracts and 'finance for assured supply' agreements (ECLAC 2011a; CBBC, 2011). Between 2002 and 2007, these donations were made up of 'natural resource'-related donations (74 per cent), infrastructure<sup>2</sup> (25 per cent), aid (1 per cent) and 'other' (Guo, 2010).

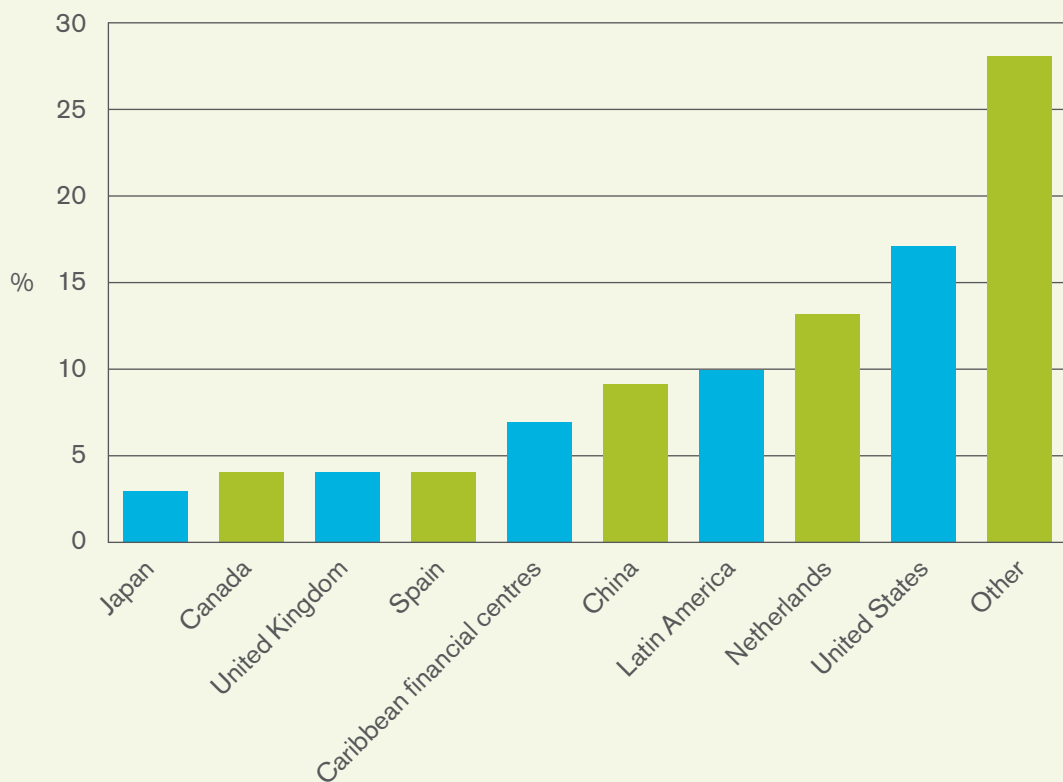
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1. China's 12th Five-Year Plan approved in March 2011 aims to strengthen the 'Going Out/Global Strategy', encouraging Chinese companies to be more competitive and invest overseas (WWF, 2012; Kotschwar *et al.*, 2012). This strategy includes the following components: in agriculture, an aim to have more South–South cooperation especially in other Asian countries, Africa and Latin America, which includes technology demonstration projects (10 centres), dispatching technologists (1350), conducting training, and joint epidemic control. The strategy also mentions increased participation in international standards development and a plan to collaborate with other countries or international organisations to develop 'environmental techniques' for domestic production. The strategy also mentions that companies should 'enhance the management to reach the international standard' and 'fulfil corporate social responsibilities benefiting local people' (Department of International Cooperation, Ministry of Agriculture, 2011).

2. According to Kotschwar *et al.* (2012: 3), 'China has also been active in infrastructure development projects in Latin America. CDB [China Development Bank] has offered a \$2.6 billion 10-year loan to revive a freight train system connecting Buenos Aires to much of Argentina's central heartland. In the country's Rio Negro province, the Metallurgical Corporation of China has invested \$80 million to reactivate an iron ore mine, and China's Beidahuang Group has promised \$1.4 billion in irrigation infrastructure in exchange for a 20-year contract to grow corn, wheat, soy, and dairy on otherwise dry land for Chinese consumers.'



**FIGURE 1: LATIN AMERICA AND THE CARIBBEAN: ORIGIN OF FOREIGN DIRECT INVESTMENT, 2010**



Source: ECLAC, 2011b

China's direct investment (defined as investment that does not come from the financial industry) to Latin America was US\$11 billion in 2010, an increase of 24 per cent from US\$8.9 billion in 2009. This investment makes up almost 19 per cent of China's direct investment globally (MOFCOM, 2011a). In 2010, exports from Argentina and Brazil to

China reached a value of US\$6.8 billion and US\$38.1 billion, respectively (MOFCOM, 2011a). Gallagher *et al.* (2012) in what they call 'highly imperfect' research, due to challenges of data availability and a lack of transparency by Chinese banks, estimate that since 2005 Chinese banks have loaned US\$75 billion to Latin America.

## TWO GROWING TRADE AND INVESTMENT BETWEEN CHINA AND LATIN AMERICA CONTINUED

While detailed and disaggregated figures on the size of investment and trade flows between China and Latin America are lacking, some information is available on who is investing, in which sectors and how.<sup>3</sup> In 2009, for example, China became Brazil's largest trade partner and this was followed by major investment announcements in 2010 (CBBC, 2011). Investments have taken the form of mergers and acquisitions, joint ventures or greenfield<sup>4</sup> investments – these types of investments are predicted to continue (CBBC, 2011). For example, WISCO, a Chinese state-owned mining company, has purchased 21.5 per cent of MMX Mineração e Metálicos S.A. (the mining company of Brazil's EBX group) for US\$400 million (CBBC, 2011).

In 2010, 93 per cent of Chinese investment in Brazil was from the 23 Central State-Owned Enterprises (SOEs), considered to be the pillars of the Chinese economy (CBBC, 2011). In the same year, 8 of the 23 SOEs announced investments reaching almost US\$22 billion mainly in the mining and agriculture (especially soy-

related) sectors in Brazil (CBBC, 2011). The trend in Brazil reflects broader patterns in China's overseas investment. In 2008, for example, almost 70 per cent of all China's overseas direct investment (non-financial) was made by SOEs<sup>5</sup> (Bulletin of Chinese Outward Foreign Direct Investment, 2008, cited in Ren, 2011). In this sense, SOEs are 'leading the way' in terms of China's investment overseas. Consequently, the analysis in this paper emphasises the role and use of standards by SOEs rather than SMEs, despite the latter being of equal interest from a development perspective.

In 2010, a third of the pulp exports from Brazil went to China (Bracelipa, 2011). It is estimated that 70 to 90 per cent of Brazilian soy will be exported to China by 2020, mainly from the state of Mato Grosso. Brazil is the world's second largest producer of soy after the US (TNC, 2011). In 2011, soybeans and soybean-related products were the main export from Brazil to China, with an estimated value of US\$11.7 billion (TNC, 2011). From 2000 to 2010, China displaced the

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3. Kotschwar *et al.* (2012) have characterised Chinese investment as follows:

- 1) Chinese investors take an equity stake in a very large already-established producer, to secure an equity-share of production on terms comparable to other co-owners
- 2) Chinese investors take an equity stake in an up-and-coming producer to secure an equity-share of production on terms comparable to other co-owners
- 3) Chinese buyers and/or the Chinese government make a loan to a very large already-established producer in return for a purchase agreement to service the loan
- 4) Chinese buyers and/or the Chinese government make a loan to finance an up-and-coming producer in return for a purchase agreement to service the loan.

4. A form of foreign direct investment investment where a parent company starts a new venture in a foreign country by constructing new operational facilities from the ground up.

5. In 2008, 20.1 per cent of China's overseas investment was made by limited liability companies and 6.6 per cent by 'companies limited by share' (Bulletin of Chinese Outward Foreign Direct Investment, 2008, in Ren, 2011).

European Union as the main destination of Brazilian soybean exports, its market share rising from 15 per cent in 2000 to 53 per cent in 2009 (TNC, 2011). It has been argued that this demand will not be met by increased productivity – an expansion of land under production is thought to be necessary (TNC, 2011). The Brazilian Government predicts that a total agricultural expansion of 9.7 million hectares will take place between 2010 and 2020 – 4–5 million hectares of which is predicted for soybean production (TNC, 2011).

In Chile, the situation is similar. China is now Chile's largest trading partner with exports, mainly from the mining and forestry sectors, totalling over US\$17,356 million in 2010 (DIRECON, 2011). In 2010, 23 per cent of Chile's total exports went to China, of which 42 per cent was of copper and copper-related products (ECLAC, 2011a). This can be partially attributed to the partnership between Minmetals (a Chinese mining SOE) and Codelco (Chile's national copper corporation). Codelco is the largest producer of copper and associated products in the world and this partnership is one of China's most significant in the region. One-tenth of Chile's total agricultural and forestry exports went to China in 2011 (ODEPA, 2012a). This trade is expected to expand further, particularly in the export of agricultural products such as fruit, as well as wine and meat (DIRECON, 2011).

In Peru, Chinese investment has focused on the mining sector, with one functional project operated by Shougang Hierro Peru and one ready to begin, operated by Aluminium Corporation of China Limited (Chinalco). Both of these are Chinese mining SOEs that have obtained a majority stake in Peruvian companies operating mines in the regions of Marcona and Morococha, respectively.<sup>6</sup> Shougang's project, in the region of Marcona, is operational and expanding. Shougang Hierro Peru is China's first major investment in Peruvian mining (Kotschwar *et al.*, 2012). Chinalco's project, in the region of Morococha, has an approved Environmental Impact Assessment (EIA) and the project is ready to start. Communities are being moved to a new town that has been built for communities who had to be resettled (see Case Study 1).

Additionally, there are five Chinese projects in the process of exploration in Peru.

China is now the most important player in the global trade of wood products: it is the largest exporter of value-added wood products (e.g. wood flooring and furniture), and the largest importer of unprocessed or semi-processed wood (logs and lumber). This is partly because there is a limited supply of domestic timber due to China's logging quota (Ganguly and Eastin, 2011). China imports pulp and paper from Brazil and Chile, as well as logs and plywood from Brazil (Ganguly and Eastin, 2011). Although 'the proportion of South American timber in the Chinese market is vanishingly small', Chinese demand is hugely significant for Peru – China is now Peru's largest timber-trading partner and the biggest importer of Peruvian timber (Putzel, 2009: 1). In 2009, the second, third, and fourth largest exporters of Peruvian timber were Chinese-owned companies (Peru.com, 2009 in Putzel, 2009).

It is clear that investment and trade between China and Latin America is growing. This investment and trade takes different forms, as discussed further in the rest of this paper. These forms in turn shape the adoption of sustainability standards and the nature of attempts to address some of the sustainability challenges outlined in Section 3.

While trade with China may be very significant for certain commodities and countries in Latin America, with China being one of the major drivers of exports (for example, timber exports from Peru), these exports may be very relatively small in terms of China's overall consumption and imports. This imbalance poses a challenge in terms of researching and fully understanding or appreciating, particularly from the Chinese perspective, the possible implications and significance of this trade for particular countries and for sustainability more broadly.

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6. Chinalco is owned by central government, governed by SASAC (the State-owned Assets Supervision and Administration Commission of the State Council, China); Shougang is owned by the Beijing government and governed locally. They are both dominant players in their industries of aluminium and steel.

# THREE SUSTAINABILITY CHALLENGES AND OPPORTUNITIES IN CHINA–LATIN AMERICA TRADE AND INVESTMENT

This section presents some of the main opportunities and challenges posed by the growing trade between China and Latin America. It aims to set the scene for better understanding of the potential need for, and value of, existing and future sustainability initiatives.

Economic growth, infrastructure development and job creation are some of the main benefits of this trade (TNC, 2011). A further benefit is access to credit, possibly otherwise unobtainable for some Latin American countries (such as Venezuela, Argentina and Ecuador) (Downs, 2011 in Kotschwar *et al.*, 2012). The development of new facilities such as soy processing and new roads has been a significant benefit.

However, a lack of environmental and social legislation and enforcement by national governments has often left a 'governance gap'. This has led to concerns around environmental sustainability and lax environmental standards, depletion of natural resources (e.g. deforestation), labour exploitation, poor working conditions, and possible negative ramifications for local communities who may be displaced or experience a loss of livelihoods – although many of these challenges are not unique to trade between developing and emerging economies. But there is a vital need to balance economic growth with improvements of livelihoods of the poor as well as protection of natural resources.

## 3.1 GOVERNANCE AND TRANSPARENCY

There are concerns about the impact of Chinese investment on local governance standards. Kotschwar *et al.* (2012: 2) cite UNCTAD's *World Investment Report* (2007) which notes that:

*non-OECD investors – most prominently Chinese investors, operating under a doctrine officially labelled 'noninterference in domestic affairs' – have often undermined hard-won governance standards observed by multinational corporations subject to home country legislation that conforms to the OECD Convention on Combating Bribery (including the US Foreign Corrupt Practices Act), and ignored or bypassed the best-practice environmental standards insisted upon elsewhere. (UNCTAD, 2007 in Kotschwar *et al.*, 2012)*

Gallagher *et al.* (2012: 1) argue in relation to loans that: 'Chinese banks impose no policy conditions on borrower governments but do require equipment purchases and sometimes oil sale agreements', and 'Chinese finance does operate under a set of environmental guidelines, but those guidelines are not on par with those of its Western counterparts.' These concerns are not always justified, however, with a recent report by Irwin and Gallagher (2012: 1) arguing that 'high social and environmental costs are endemic to mining in Latin America' and that

Chinese<sup>7</sup> companies do not necessarily perform any worse than their foreign and domestic counterparts. Cerutti *et al.* (2011) have similar findings in their research of Chinese companies in Cameroon, Africa, where the nationality of logging companies (European or Chinese) does not have a great impact on sustainability outcomes. The regulatory context of Cameroon is a far stronger determinant of company behaviour than the countries of origin. Chinese *demand* for tropical logs, on the other hand (in terms of sheer scale), is very significant in determining forest management and local livelihoods.

China has rejected the Extractive Industries Transparency Initiative (EITI) (Kotschwar *et al.*, 2012) and is not a member of any partnership-based sustainability initiatives, such as the International Council for Mining and Metals (ICMM)<sup>8</sup> (Kotschwar *et al.*, 2012), though China Minmetals Corporation<sup>9</sup> is a controlling shareholder of the Minerals and Metals Group (MMG), a company headquartered in Australia and operating globally, which is a member of ICMM. Where Chinese companies are operating in countries that have signed up to EITI (e.g. Peru), China has been criticised for not participating.

Kotschwar *et al.* (2012) compares the behaviour of two OECD and two Chinese mining companies in Peru. They find that the main

Chinese mine in Peru – Shougang Hierro Peru – is not accountable to external shareholders, does not participate in international forums, is lacking transparency, and has shown little willingness to improve its practices so that they meet international standards. Irwin and Gallagher (2012) on the other hand, use new government data and historical archives to demonstrate that while ‘Shougang performed poorly on many indicators, [but] when compared to other foreign and domestic mining companies its poor performance has not stood out in recent years.’ They attribute the problem to poor governance in Peru, since ‘the Peruvian government has continually failed to force mining companies to comply with their investment commitments, respect government and global standards, or negotiate with their unions’ (Irwin and Gallagher, 2012: 1).

Indeed, a lack of transparency in the operations of Chinese SOEs has been an issue in the mining sector in Peru but is seen to be less of a problem in Brazil and Chile where Chinese SOEs have partnered with well-established local companies (because of host-country foreign-investment requirements) and implemented more substantive sustainability agendas, and where legislation is arguably more stringent (and/or better enforced). Evidently nation-states like Peru cannot count on foreign or domestic firms to self-regulate (Irwin and Gallagher, 2012: 1).

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7. We adopt the same definition as Cerutti *et al.* (2011: 24) of ‘Chinese companies’: any company headquartered in mainland China, including in the Hong Kong Special Administrative Region. Companies with ethnic Chinese owners of any nationality but without headquarters in China are not considered Chinese companies.

8. Mining companies and associations become members of ICMM. ICMM brings together 21 mining and metals companies as well as 31 national and regional mining associations and global commodity associations. These 21 member companies employ 800,000 of the estimated 2.5 million people working in the mining and metals sector, with interests at over 800 sites in 62 countries across the globe, and exploration activities that extend far beyond this. As part of this membership, companies commit to implement the ICMM’s Sustainable Development Framework: a set of 10 principles to be integrated into corporate policy and reported on each year. Companies’ progress is evaluated annually and published through the ICMM’s website (Kotschwar *et al.*, 2012; ICMM, 2012).

9. A major multinational state-owned enterprise.

### 3.2 ENVIRONMENTAL CONCERNS

Environmental concerns associated with growing trade in natural resources include deforestation, loss of biodiversity and pollution. In Brazil, for example, China's growing demand for soy has led to fears of increased deforestation. While global demand for soy has been growing significantly, it is Chinese demand that stands out: in 2009 China was importing over 50 per cent of Brazil's soy, with China predicted to be buying up to 90 per cent of Brazilian soy by 2020 (TNC, 2012). This is of particular concern because, at present, the Chinese market appears unconcerned about environmental footprints and indifferent to certification (TNC, 2012). In a controversial process, Brazil's Forest Code – the legislation that governs agricultural production and land use in Brazil – is being reformed (*New York Times*, 2012). Under the new code, partially vetoed by Brazil's president Dilma Rousseff, protection of sensitive areas and the required amount of forest preserved along riverbanks will be reduced (*The Guardian*, 2012b). While the agribusiness sector is one of the parties promoting the code (and this sector will ultimately benefit from the growing market for soy in China), the extent to which these changes are directly fuelled by the increase in Chinese demand for soy remains unproven.

Illegal forestry is generally regarded as a significant driver of deforestation (Ganguly and Eastin, 2011). 'China' as well as 'Chinese loggers' have been criticised for their role in illegal logging (see Laurence, 2012; Putzel, 2009), although sometimes these criticisms are biased or ill-informed (Mawdsley, 2008; Putzel *et al.*, 2008 in Putzel, 2009). One report estimates that 75 per cent of logs harvested illegally in Myanmar, Congo, Equatorial Guinea, Gabon, Papua New Guinea and the Russian Far East end up in China

(Ganguly and Eastin, 2011). Evidence suggests that this situation has now improved – with a significant decline in Chinese log imports from most of these countries, whereas log imports from developed countries where illegal logging has not been a concern (such as New Zealand, Australia, Canada and the US) increased substantially after 2007 (Eastin *et al.*, 2012). This has been attributed to a 'more responsible approach to sourcing logs by the Chinese wood products industry', in part driven by the legislative changes to timber sourcing in the US and EU (see Section 4.3) (Eastin *et al.*, 2012: 11).

### 3.3 EMPLOYMENT, LIVELIHOODS AND COMMUNITY IMPACTS

Evidence from a number of case studies analysed for this research suggests that the impact of this trade and investment on employment and livelihoods is mixed. In general, it is associated with increases in overall employment – though the 'quality' of this employment inevitably varies (see Case Studies 1–4). Sometimes, labour at particular levels (managerial or financial) may be 'imported' while local employment at other levels (i.e. non-managerial, manual labour) expands. Other livelihoods may be displaced. This is not to say that this is necessarily unique to trade between Latin America and China – similar trends can often be observed in 'North–South' trade.

The four case studies in this section exemplify some of the Chinese investments taking place in Latin America, and their impacts on local communities and livelihoods.

## CASE STUDY 1: CHINALCO MINING AND ITS TOROMOCHO MINE IN PERU

Chinalco's Toromocho mine project offers one example of Chinese mine development in Latin America. Chinalco Mining is a publically listed company, based in Beijing but listed on the Hong Kong stock exchange (Bloomberg, 2013). It is the overseas non-aluminium and non-ferrous metals arm of aluminium giant Chinalco – a Chinese state-owned enterprise (SCMP, 2013).

Work to construct the mine began in 2012 and as of January 2013, was still ongoing. Full production is expected to begin in late 2013 (SCMP, 2013). The mine is expected to provide 5000 new jobs, and involves the relocation of the city of Morococha (population 7890). Chinalco has started the construction of a 'new Morococha' where people (mostly workers) will be able to own their house and, (according to Chinalco) will have access to schools, hospitals, churches, etc. It will also be highly accessible – as part of their 'inclusion' policy – and all roads will be paved<sup>10</sup> (Chinalco, 2012). It was completed in 2011 (SCMP, 2013). In December 2012 some people were moving into the new town, but several hundreds were still reluctant to go (*The Guardian*, 2012a).

Chinalco has implemented a consultation process with the local community as part of its environmental impact study and implemented a corporate social responsibility programme that includes a social fund 'Fondo Social Toromocho' (Chinalco, 2012; Kotschwar *et al.*, 2012). This appears to signify recognition by the company of the need to obtain a social licence to operate, and lesson-learning from previous Chinese experiences in the region (see Case Study 2). This demonstrates a growing recognition of the need to move towards sustainability or to 'green' Chinese investment and to improve understanding of the social

context in which Chinese firms operate. This is consistent with China's policies for FDI, its domestic policy goals of 'green development', and as reflected in the recent development of a number of guidelines for foreign companies investing in China and for the behaviour of Chinese investors overseas, as well as investor requirements (see Section 4.2, for more analysis). Toromocho secured a \$21 billion loan from the China Export and Import Bank (CEIB), subject to the 2007 CEIB Guidelines for Environmental and Social Impact Assessments, 'requiring that borrowers follow host country laws and regulations and specifying the need for social and environmental assessments for overseas projects' (Kotschwar *et al.*, 2012: 14).

However, not all the residents of Morococha are satisfied with the resettlement plans, and there are concerns about the effectiveness of the consultation process. Some community members and the town's mayors are worried about the safety and quality of the new town that has been selected for them, and are dissatisfied with compensation agreements (BBC, 2008; FT 2011). This has resulted in accusations regarding the transparency of the resettlement, which led to protests in 2010 (FT, 2011).

Resettlement is being managed by the firm, but had faced several challenges – including a refusal by the regional government to give the company a building permit for the new town and an order by the town's government to stop the new town's construction. The firm filed a constitutional claim and a judicial claim against the government. The firm obtained a preliminary relief that allowed construction to go ahead but claims are still pending. If the firm is ruled against, the resettlement may be delayed or halted altogether (SCMP, 2013).

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10. According to Kotschwar *et al.* (2012), Chinalco has agreed with the Transport and Communications Ministry (MTC) and Colombian Sociedad Desarrollo Vial de los Andes (Deviandes) to rebuild 10 kilometres along a stretch of the Centro IIRSA highway that is on the Toromocho concession, at a cost of US\$20 million.

## CASE STUDY 2: SHOUGANG MINING COMPANY IN PERU

Shougang Corporation, a state-owned enterprise, is one of China's largest steel companies. The company operates in Peru as Shougang Hierro Peru (referred to from now on as Shougang). It operates the Marcona Mine in the Marcona District, an open-pit iron mine acquired in 1992.

Shougang has been accused of poor social and environmental behaviour in Peru from the outset, and has been fined numerous times for polluting the environment, and inattention to worker safety and health. It has been subject to years of contentious strikes by the Peruvian labour force (Kotschwar *et al.*, 2012). The company is accused of paying far lower wages than its competitors and the lowest in Peru – miners complain that wages at Shougang are among the lowest in Peru's multi-billion dollar mining industry, at an average \$14 a day. The average miners' salary in Peru is \$33 a day, according to Peru's National Society of Mining, Petroleum, and Energy (Kotschwar *et al.*, 2012).

Shougang reportedly reneged on its commitment to invest \$150 million in the community – it spent only US\$35 million and paid a US\$14 million fine instead (Kotschwar *et al.*, 2012). Shougang's sustainability agenda is limited to some community programmes which are focused on monetary and other donations (e.g. computers for schools) and compliance with local standards of environmental quality. Shougang Hierro Peru's activities have highlighted the lack of

regulation and enforcement of the mining sector in Peru. This has been attributed to institutional and regulatory weaknesses (such as government organisations having overlapping duties) and an accusation that the Peruvian government is primarily focused on attracting investment, rather than asking who the investors are and regulating them effectively.

Lanegra, the Director of Peru's independent human rights Ombudsmen has argued that: 'the Environment Ministry, not the Ministry of Energy and Mines, [should be] responsible for approving environmental impact studies for these projects. It should be a distinct entity within the environment ministry that has full funding and independence.' (FT, 2011)

One interviewee from a Peruvian NGO argues:

*There are also a number of systems [In Peru] that make the advancement of legislation very complicated... It is worth mentioning that the Ministry of Energy and Mining uses the number of EIA approved per year as an indicator of success. This reflects the 'quantity not quality' approach of the current legislation... Furthermore the current system for Environmental Impact Assessments is obsolete and should no longer be used. It evaluates projects on an individual basis and does not take into account cumulative impacts of operations. These assessments are never technically supported or evaluated by third parties.*



### CASE STUDY 3: CHINESE PROJECTS TO ASSURE SUPPLY OF NATURAL RESOURCES IN LATIN AMERICA

In Brazil, the collaboration between governments and Chinese SOEs may be seen in the case of the Chongqing Grain Group, a Chinese SOE, and the government of the state of Bahia. In 2011, Chongqing Grain Group announced a US\$4 billion investment for a new 100-hectare soy processing plant to be built in Barreiras (Bahia) on land donated by the local authority. In an interview with *Valor Economico* (2011), a renowned Brazilian business newspaper, Bahia's Secretary of Agriculture highlighted the importance of assured supply for China and how this project would allow Chongqing Grain Group to control its soy supply. This development may offer greater employment opportunities and allow Brazil to add value to its soy, although tangible benefits remain to be seen.

In Chile, in 2006, Minmetals (another Chinese SOE) agreed to pay US\$500 million to Codelco in exchange for a 55,750 tonne supply of copper per year for 15 years (ECLAC, 2011a). The agreement included the option for Minmetals to buy up to 49 per cent of Codelco's Gaby mine. In September 2008, after a wave of local criticism and fears of nationalisation, Codelco announced the interruption of the deal. Minmetals gave up the purchase of the stakes and did not seek compensation, avoiding future problems with local communities, the workers and the Chilean government (ECLAC, 2011a). This case reflects some of the challenges and difficulties faced by Chinese investors in Chile and in new environments more broadly.

#### CASE STUDY 4: RIO BLANCO, ZIJIN MINING GROUP LTD, PERU

Peru offers an example of some of the conflicts resulting from Chinese investment in mining and mining operations, and the importance of host-country legislation in shaping the impacts of investment.

The Rio Blanco mining project in Peru is 90 per cent owned by Chinese SOE Zijin Mining Group Ltd. From the outset there was strong opposition to the mine's development, due to concerns over environmental and social consequences for the local community. Located in the cloud-forest region of the Huancabamba mountains, the project was predicted to have serious consequences for important and fragile ecosystems. It would involve the displacement of agriculture in the area, leading to knock-on effects for farmers and the local economy (Oxfam America, 2009). The company disregarded concerns and began explorations without a 'social licence to operate', either informal or formal. The formal requirement is to satisfy the Peruvian law that approval should be obtained from two-thirds of the citizens of the area (Oxfam America, 2009). This led to strong opposition from communities and NGOs, which resulted in allegations of human rights violations from Rio Blanco and of insufficient support from the government.

In 2008, Rio Blanco announced that the government had granted it permission to start operations within 50km of an international border, which is illegal under Peruvian law (Oxfam America, 2009). In the same year, the company was fined for starting operations without permission and for polluting water sources. Rio Blanco was due to present its Environmental Impact Assessment in January 2009, which did not happen, with a view to starting operations in 2011 despite a rejection of mining by a number of

communities (in the form of protests). In 2011, Zijin presented two letters apologising for its previous behaviour, hoping that its relationship with the community could improve. The local communities answered this letter and rejected Zijin's actions with a document called 'the 7 truths about Rio Blanco'.

In an interview with the Financial Times, Dr Cynthia Sanborn of Universidad del Pacifico raised concerns that the government in Peru is more focused on encouraging investment than on regulating companies, understanding the companies or even preparing communities for the presence of new mining firms (FT, 2011). Local communities and civil society have been demanding more help from the government to deal with issues with the Chinese mining companies and the mining industry in general, but the government appears to be caught in a conflict of interest. The legislation-enforcing body is also in charge of attracting Chinese investment.

Ruben Gonzales-Vicente, a PhD student from Cambridge University, specialising in Chinese mining and its investments in Latin America, explains the perception that the:

*'Rio Blanco project was sold for 'cheap' because of the conflict associated with it. However, Zijin seems to have paid too much considering all the unrest and conflict. When Zijin took over the Rio Blanco project, they thought that the Peruvian government would be able to deal with the social part, as the state would have done in China. When this did not happen, they [Zijin] realized... that they would have to deal with the issue themselves.'* (IIED interview, 2012)

Evidently, the Peruvian context has posed a new challenge for Chinese companies. Local communities and NGOs have played an active

role in making sure that Peruvian legislation is enforced. An interviewee from a well-known Peruvian NGO states that 'The involvement of local communities has resulted in increased pressure for the Ministry of Energy and Mines to demand the right and up-to-date permits.' (IIED interview, 2012)

Indeed, growing tension between mining companies and communities, along with increased involvement of NGOs in the mediation process, has resulted in some arguably positive developments – for example, the law on the Right to Prior Consultation for Indigenous or Native Peoples was passed by Peruvian Congress in 2010 (Kotschwar *et al.*, 2012). This law requires that local communities are consulted on any regulatory change that may affect them. In addition, companies must now present their mandatory environmental impact assessments at public meetings – local people can then ask questions and voice objections, which should be taken into account. It is assumed that, in Peru, a project that does not obtain a social licence will not be able to proceed (Kotschwar *et al.*, 2012).

Peru also implemented the law for Corporate Social Responsibility in the mining sector in 2006 (Kotschwar *et al.*, 2012). This allows 50 per cent of the taxes collected from mining to go back to local communities in the form of investments in education and social programmes. Additionally, there is the voluntary initiative Mining Solidarity with the People (PMSP) where companies donate funds to improve the quality of life of communities in the areas where they operate (Kotschwar *et al.*, 2012).

In conclusion, the social and environmental record of Chinese mining companies in Latin America is mixed (Kotschwar *et al.*, 2012), but significant opportunities exist for improving sustainable development outcomes.

Research is needed to understand the extent to which these mandatory and voluntary initiatives are being implemented and being applied specifically to Chinese investors in Latin America.

# FOUR

# STANDARDS TO IMPROVE THE SUSTAINABILITY OF CHINA–LATIN AMERICA TRADE AND INVESTMENT

The sustainability of trade and investment between China and Latin America varies by country and sector, as do the drivers for the adoption and implementation of sustainability standards. In this section, we present some initial insights into the mechanisms being used in mining, forestry and agriculture and the drivers for their implementation – with a particular focus on private voluntary sustainability standards. There are also several cross-sectoral ‘standards’ that shape Chinese investment in, and procurement of, natural resources in Latin America; we look first at these.

## 4.1 CROSS-SECTORAL STANDARDS

This section offers a brief overview of some of the major standards and principles that apply to Chinese investment and procurement. These are not specific to any particular sector, but have the potential to affect the behaviour of Chinese investors overseas and the Chinese government’s purchasing decisions – and therefore have possible ramifications for the nature of investment and trade with Latin America.

This section looks mostly at the range of national investment standards in China. However, there are also some cross-sectoral international standards and initiatives relevant to both Latin American and Chinese investors. Examples include the Equator Principles, OCED Guidelines for Multinationals, United Nations Global Compact, UNEP Principles for Responsible Investment, and the UNEP Finance Initiative. However, in-depth discussion of these is beyond the scope of this paper, which focuses on

Chinese national and private corporate sustainability standards.

### Guidelines on Investment Overseas

This series of guidelines was first published by China’s Ministry of Commerce, the National Development and Reform Commission (NDRC) and the Ministry of Foreign Affairs in 2004, but has been updated annually since 2009:

*The guidelines were to make our enterprises to adopt the approach of mutual benefit, win-win, and mutual development, to combine their own multinational operation needs with industrial development goals and development priorities of host countries, avoid blind investment, and ceaselessly improve sustainable development of overseas investment of our enterprises. (MOFCOM, 2011b: 1)*

They currently apply to 115 host countries (MOFCOM, 2011b). The guidelines provide domestic companies with in-depth advice on the laws, regulations and policies concerning industrial development in these countries and encourage enterprises to evaluate their own strengths. They provide relevant information about bilateral investment-protection agreements and treaties for the avoidance of double taxation

In relation to sustainable development, the guidelines offer specific ‘reports’ on environmental factors in the countries in which Chinese enterprises may invest. For example, the country guide for the Democratic Republic of Congo outlines the country’s environmental laws and provides tips for establishing good relationships with the recipient country (Huang and Wilkes, 2011). However, it does not appear to

offer any guidance on sustainable-development-related issues beyond environmental laws. Further information is required on the extent of use of these guidelines and the degree to which they have shaped the nature of Chinese investments in Latin American countries.

### **'Green credit' guidelines**

A more recent development is China's green credit guidelines. These were issued in February 2012 by the China Banking Regulatory Commission (CBRC), specifying that Chinese 'banks shall effectively identify, assess, monitor, control and mitigate environmental and social risks'<sup>11</sup> and 'disclose information as required by laws and regulations and subject themselves to market and stakeholder supervision'. Based on the CBRC guidelines, banks will 'publicly commit to adopt international best practices or standards for overseas projects' (SynTao, 2012). The guidelines are to be applied to policy banks, commercial banks, rural cooperative banks and rural credit unions established within China. It has

been predicted that implementation will be challenging, but that the move is very significant (Zadek, 2012). CBRC is responsible for the supervision and administration of banks' green credit operations, and E&S risk management.

The China Development Bank (CDB) – one of the biggest overseas investors in China, and a significant investor in Latin America – has been involved in the development and implementation of the green credit guidelines:

*CDB participated in the formulation of the Green Credit Policy promulgated by CBRC, mapped out its 2011 working plan on loans for environmental protection, energy conservation and emission reduction, released the document specifying the indicators for environmental impact assessment for loans, introduced the environmental veto power into its credit and lending decisions and ensured all loan projects having passed the environmental impact assessments. (Bank Track, 2012)*

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11. The IFC has interpreted the guidelines as follows: 'E&S risks as used in the Guidelines refer to potential impact and risks brought to the environment and communities by banks' clients and their primary supply chains through construction, production and operational activities, which include such E&S issues as energy consumption, pollution, land, health, safety, resettlement, eco-system protection, climate change, etc' (IFC, 2012). The guidelines are quite specific: 'Banks shall develop a client E&S risk rating standard to assess and categorize clients' E&S risks. The assessment and categorization results shall become important basis for clients rating, credit approval, portfolio management and exit decisions. In addition, based on such results, banks shall take different risk management measures during the 3 checkpoints of the lending cycle (due diligence, credit review and portfolio review), and in loan pricing, setting of risk-adjusted return target and allocation of economic capital. Banks shall develop a list of clients with major E&S risks. Such clients shall be requested to develop and implement action plans for major risks involved, put in place comprehensive and effective stakeholder communication mechanisms and seek risk mitigation measures, for example through a third party sharing of potential environmental risk. Banks shall create a mechanism that encourages green credit innovation. Banks shall promote innovation in green credit business process, products and services under the premises of effective control of risks and sound commercial viability. Banks shall improve E&S performances of their own operations, put in place relevant systems, emphasise green credit awareness raising, standardize business conducts, promote green office and improve resources efficiency.' (IFC, 2012: 3).

## FOUR STANDARDS TO IMPROVE THE SUSTAINABILITY OF CHINA–LATIN AMERICA TRADE AND INVESTMENT CONTINUED

The guidelines have been well received by Chinese civil society representatives<sup>12</sup> who have congratulated the China Banking Regulatory Commission on: 'introducing for the first time [in China] the idea of risk assessment and precaution... and the assessment of social risks' (Greenwatershed *et al.*, 2012: 1). They state that the guidelines offer real potential to:

*enhance environmental and social risk management of overseas projects before issuing credit in order to ensure that the implementers of those projects abide by a country's or area's relevant laws and regulations related to environmental-protection, land, healthcare, security, etc... and adopt international practices or international norms for overseas projects applying for loans. This reflects the urgent environmental needs of China's 'going out' strategy and complies with the host countries' requirements and the call from local people. (Greenwatershed *et al.*, 2012: 1)*

But they argue that the policies cannot be fully implemented without public oversight and without supervision of stakeholders such as NGOs and the general public. Greenwatershed *et al.* (2012) note that, although the guidelines mention assessment of social risks, there is a lack of recognition of the relationship between the borrower and the concerned community.

Borrowers should ensure community involvement and offer a clear channel and mechanism for complaints. They suggest that 'evaluation and accountability of banks should include opinions from impacted people and communities' (Greenwatershed *et al.*, 2012).

Despite this lack of specificity in some areas, the guidelines do offer potential in terms of positively shaping Chinese investment. To date, to the authors' knowledge, no substantive research has been carried out on the uptake and impact of the guidelines. This will be important in the short and long term, and as a means of facilitating civil society oversight and public participation.

### China's Export–Import Bank Guidelines for Environmental and Social Impact Assessments

In 2007, the China Export–Import (EXIM) Bank (one of China's 'policy banks'<sup>13</sup>) issued a document entitled 'Guidelines for Environmental and Social Impact Assessments of the China Export and Import Bank's Loan Projects', outlined in Box 1. The China EXIM bank is one of China's biggest international lenders along with the China Development Bank.<sup>14</sup> Gallagher *et al.* (2012) estimate that since 2005, the China EXIM bank has made loans of the value of US\$9 billion to Latin America. The research by Gallagher *et al.* is

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12. In a letter to the China Banking Regulatory Commission jointly signed by Greenwatershed, Greenovation Hub, Friends of Nature, Green Earth Volunteers, China Development Brief, Global Environmental Institute, Institute of Public & Environmental Affairs, Chongqing Green Volunteer Association and Panzhuhua Hengduashan Research Society, in March 2012.

13. Meaning the bank is a tool of government, designed to support the government's policy objectives (Bräutigam, 2009, in Gallagher *et al.*, 2012).

14. In 2011, China EXIM Bank's loans totalled 914,301,463.23 Chinese Yuan Remnimbis in 2011, or approximately US\$145 million (based on 2011 exchange rates) but no information is given on the geography of these loans and to what extent they are overseas loans (or related to Latin America).

### BOX 1: CHINA EXIM BANK'S GUIDELINES FOR ENVIRONMENTAL AND SOCIAL IMPACT ASSESSMENTS

Companies investing/operating overseas with a loan from China EXIM bank should abide by the following 'principles'.

1. Carry out an EIA (this should be done during the pre-loan and loan-period review period).
2. Adhere to the host country's environmental policies and standards... obtain corresponding environmental permits. When the host country does not have a complete environmental protection mechanism or lacks environmental and social impact assessment policy and standards... refer to our country's standards or international practices.
3. Respect the local people's rights to land and resources, and properly handle the resettlement problems.
4. For the projects that have serious negative impacts on the local environment... openly consult the public in accordance with the host country's requirements.

Source: International Rivers, 2008

'exploratory' because the China EXIM bank does not publish detailed figures of its loans. China EXIM banks' loans in Latin America were heavily concentrated in Venezuela, Brazil, Argentina, and Ecuador.

While it is reassuring that Chinese investors are required to abide by 'international practices', should a host country lack legal requirements to

address environmental and social impacts, the guidelines make no mention of relevant 'international practices' or give an indication of how to assess whether a country has a 'complete environmental protection mechanism'. This is presumably up to the company's discretion with some oversight from the bank. The guidelines also explain that 'China EXIM Bank, if necessary, can require the inclusion of environmental and social responsibilities in the loan contract, in order to monitor and restrain the behaviour of borrowers'. This implies that, apart from the requirement to comply with the host country's environmental regulations, the bank will not necessarily specify that the project has to deliver social and environmental benefits (though it can if it so decides), and that consultation with local communities is required only where impacts are anticipated to be 'seriously' negative. It is unclear to what extent the bank requires its lenders to meet certain environmental and social responsibilities (i.e. number of cases and nature of these responsibilities).

In terms of monitoring compliance with the guidelines, the bank explains that 'China EXIM Bank shall inspect and monitor the project's construction and operation, based on the results of environmental and social impact assessments' and:

*for projects under construction, the borrowers or project owners should regularly report to the China EXIM Bank the actual impacts on the environment and society brought by project construction, and the status of implementation measures in eliminating and controlling these impacts. If the requirements are not met, China EXIM Bank has the right to require the borrowers or project owners to take timely measures to eliminate these impacts. If they fail to eliminate the impacts of the projects, the China EXIM Bank has the right to stop disbursing the loans and demand an early payback of the loan, in accordance with contract.<sup>15</sup>*

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15. The Bank's annual report has a section on social responsibility. In this, it highlights its key achievements as offering musical education for younger generations and that it 'worked jointly with officials and people of poverty stricken counties' as well as donating books and computers to schools (China EXIM Bank, 2011). Interestingly it doesn't refer to its guidelines at all, or the nature of its lending decisions.

An official of China's EXIM bank<sup>16</sup> explained that the bank *had* delayed loans in Indonesia and Malaysia because it lacked a certified environmental impact assessment. The official explained that companies with fraud and/or environmental problems could be punished by blacklisting, or there would be a permanent delay in the processing of relevant loan applications/requests for ODA. He also said that China EXIM had denied a lot of projects in Latin America, Africa and Northeast Asia.

The official explained that in all cases the bank requires environmental impact reports, and unless the report is not qualified or certified (presumably by the bank itself or a third party), they will not approve the loan. Sometimes, China EXIM will consult with 'professional people' to get their advice on the environmental impacts. A certified completion report is also required at the time of project completion and an additional report may be required during project construction. However the official said that many enterprises object to the costs of environmental impact reports. China EXIM Bank is also looking to international institutions to provide more assistance in the area of implementation – suggesting that implementation remains a challenge.<sup>17</sup>

### **Guidelines on Environmental Protection for China's Outbound Investment and Cooperation**

In March 2013, the Ministry of Environmental Protection (MEP) and MOFCOM published the Guidelines on Environmental Protection for China's Outbound Investment and Cooperation, aiming to 'standardize the overseas activities of Chinese investors on environmental protection' (Qingfen, 2013). These were developed in response to concerns about the impact of Chinese investment overseas and were seen as a key means of dealing with the environmental risks Chinese companies might face when 'going out'. Yao Jian, spokesman for the Ministry of Commerce, has said that the Guidelines will help companies 'strengthen their core competitiveness and soft power in the global market' (Yao, in Qingfen, 2013).

At present, these Guidelines are voluntary. They are designed to raise the awareness of Chinese companies about issues of religion, culture, custom, historical sites and labour rights in countries overseas. The Guidelines encourage Chinese companies operating overseas to be 'socially responsible' – for example by providing training and job opportunities for communities, driving economic growth in the local area, and community development. The Guidelines highlight the need to balance economic development and environmental protection and encourage companies to move towards low-carbon

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16. In a talk given in 2011 at a meeting about Environmental Policies on Chinese Overseas investments: [www.wri.org/event/2011/06/book-launch-environmental-policies-chinas-investment-overseas](http://www.wri.org/event/2011/06/book-launch-environmental-policies-chinas-investment-overseas).

17. The official also explained some of the motivation of China EXIM officers to act on environmental issues: on one hand, they need to address environmental issues because 'it is a rule in our bank' that the President's image must not be affected by controversy; on the other hand 'we are just bankers' and have many things to do.



development by developing their own environmental management strategy. The guidelines encourage companies to comply with local regulations and laws concerning the environment, but also to incorporate environmental protection into their own business strategies and operational plans (MOFCOM, 2013). They also emphasise the importance of internal training regarding local environmental regulations and environmental issues.

The Guidelines mention waste management, avoiding water pollution and conserving biodiversity, which should be done through collaboration with local government and communities. Ecological restoration is recommended, according to local regulations or following best industry practice.

The Guidelines recommend that companies carry out due diligence before investing overseas or merging with or acquiring companies overseas. This due diligence should include an assessment of environmental risks. Companies should procure environmentally sustainable goods where possible. The Guidelines emphasise the need to communicate with local communities, using a variety of techniques. Finally, the guidance encourages companies to learn from international organisations and multilateral financial organisations, regarding environmental protection. The Guidelines may be monitored together by MEP and MOFCOM (MOFCOM, 2013).

Clearly, these guidelines are far-reaching in terms of breadth and depth of content – and notably emphasise the need to strengthen community relations, something the Chinese companies in our case studies have struggled with – though the Guidelines do not explicitly recognise the rights of communities and human rights are absent (Bosshard, 2013). Bosshard (2013) has

compared the Guidelines to those of the OECD, and noted that the Chinese guidelines are not supported by any compliance mechanism unlike the OECD Guidelines. A compliance mechanism would help ensure that the new guidelines are actually being implemented. Indeed, their voluntary nature and the lack of clarity on how their implementation will be incentivised, facilitated and monitored leaves a large degree of uncertainty around the potential extent of their application and effectiveness.

### **Chinese policies on public procurement**

Also relevant to Chinese and Latin American trade, and the possibility of influencing purchasing decisions, are Chinese policies and standards concerning public procurement. The Chinese government officially incorporated 'green procurement' into its 12th five-year plan in 2011, 'making an innovative move in the new era of environmental protection' (CCICED, 2011: 23). Of relevance here is the 2008 law on the 'Promotion of Circular Economy' passed by the NPC standing committee which requires that the government should contribute to the objective of national economic and social policy, including protecting the environment, supporting underdeveloped regions and ethnic minority areas, and promoting SME development.

Despite these intentions, it seems that government players (regional and local) are only *advised* to make green procurement decisions, rather than being obliged by law. CCICED's report explains that:

*China's government green procurement policies lack continuity and the goals need to be further clarified. Government Procurement Law currently implemented stipulates that, government procurement should contribute to the accomplishment of the objectives in national*

## FOUR STANDARDS TO IMPROVE THE SUSTAINABILITY OF CHINA-LATIN AMERICA TRADE AND INVESTMENT CONTINUED

*economic and social policies, including environmental protection. In October 2006, MOF and MEP jointly issued Implementation Opinions on Government Procurement of Environmental Labelling Products and require that state organs, public institutions and organizations at all levels give priority to environmental labelling products in the procurement with financial fund and not purchase products harmful to the environment and human health. In comparison, developed countries such as the U.S. and EU have the explicitly legislations on government procurement of ecological, environment-friendly products and services.... Comparatively speaking, the role of the Chinese Government in leading terminal green consumption is rather weak, and the mandatory feature of government procurement of environment friendly products is not highlighted. (CCICED, 2011: 36)*

However, the report also explains that the Chinese government is working to improve its environmental credentials to ensure that Chinese products are not discriminated against in international trade – the adoption of standards is regarded as a way to improve international competitiveness and avoid ‘trade protectionism dressed in environmental protection’ (CCICED, 2011: 25) and to help avoid environmentally unsustainable products from entering China:

*To this end, China further enhances its environmental standards and develops low carbon certification standards, and initially sets up its own green line of defense through mutual recognition with developed countries. (CCICED, 2011: 25)*

Ensuring that these standards do not exclude SMEs and small-scale producers both within China and from developing countries trading with China will be important. Some local governments

(such as Tianjin) have, however, recognised this need explicitly, by incorporating a preference for SMEs in their procurement policies. In Tianjin, eco-friendly, energy-efficient products, innovative products, national industrial products and products of SMEs are given priority in the procurement process.

CCICED explains that there is still a great deal of progress to made on environmental policies:

*there is an absence of targeted laws, regulations, policies and specific industry certification standards. In a comparison with developed countries, not only did economic incentives and innovative mechanisms relate to green supply chain development, but also appropriate monitoring and punishment mechanisms have not in place. (CCICED, 2011: 36)*

Enforcement of environmental laws that do exist remains a key challenge, since the cost of pollution/environmental damage is typically less than the costs of sanctions, and less than choosing a ‘better’ environmental option.

As the Chinese government works towards improving environmental legislation and enforcement, it will be important to ensure that attempts at ‘greening’ or formalisation do not have negative consequences for the inclusion of small-scale producers who dominate much of China’s production and processing in agriculture and forestry. The risk of not doing so could be increased inequality and social costs – as evidenced by China’s attempts to green its dairy sector by producing ‘cow hotels’ (Mo *et al.*, 2012). Tianjin offers an example of meaningful attempts to balance environmental and development factors, although the extent to which the Tianjin government has been able to implement its procurement policy effectively is unclear.

## 4.2 SUSTAINABILITY STANDARDS IN MINING

The mining industry is distinct from the agricultural and forestry sectors. The scale of most mining operations and their impacts (and the need for large investments/investors) also means it is easier in mining than in agriculture to observe operations and the implementation of standards. Obtaining a social licence to operate is increasingly important for mines to be able to open and remain functional. Implementing social and environmental standards can be one tool to help obtain a social licence to operate (Buxton, 2012).

However, a researcher from a large Peruvian university has argued that mining firms 'try to reduce costs and increase profit margins, and avoid international condemnation by complying with fair standards to the extent it doesn't cost them too much' (IIED interview, 2012). Several factors determine the extent to which standards are implemented. One Chinese SOE – one of the largest coal suppliers in the world – has explained that price and quality are the overriding decision-making factors in sourcing mineral supplies. Anecdotal evidence<sup>18</sup> suggests this is the case for other Chinese companies also. This SOE tends to source its supplies from agencies, rather than directly from mines. Presumably it is therefore unknown or unclear to what extent any standards are applied at the production stage – and perhaps also irrelevant if price and quality are most important.

This SOE's coal exploration projects may have 'environmental certificates' where the local government requires it (e.g. in Australia) but this

varies according to national/local legislation. This trend has also been observed in Latin America. One interviewee, an expert in Chinese mining companies in Peru, explains that

*Chinese companies are in the business to try and reduce the cost of their own metals and what they do with the metals. There may be competition when it comes to buying a project but after that not really. (IIED interview, 2012)*

He implies that standards and sustainability more broadly are not, currently, deciding factors in procurement and extraction – cost is the overriding decision-making factor in and the main basis on which companies compete (standards are not yet being used as a point of differentiation in terms of companies' reputations).

A number of buyers and representatives from Chinese companies interviewed for this research – including a number of large state-owned and private companies in the mining and agriculture sectors (see Appendix 1) – reaffirm that there is a growing emphasis on quality in purchasing, but not much, if any, consideration of sustainability. Some environmental and social standards may be met incidentally (suppliers are applying these standards for other markets or driven by domestic regulation/standards) but not as a direct result of Chinese purchasing pressure or decisions. A buyer from a leading mining and minerals SEO in China explains that the

*Chinese government has not published any policies regarding sustainability on importing of this [Chromium] product... Choosing new suppliers does not depend on any sustainable certification, only price. (IIED interview, 2012)*

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18. IIED (2012) Interviews with other SEOs and mining companies in China: See Appendix 1.

## FOUR STANDARDS TO IMPROVE THE SUSTAINABILITY OF CHINA–LATIN AMERICA TRADE AND INVESTMENT CONTINUED

The case studies in Section 3 demonstrate that Chinese SOEs in the Latin American region are generally attempting to maintain and/or improve their relationships with relevant stakeholders and vice versa. But they are operating in a very different political, environmental and cultural context – both when compared to the Chinese context as well as between different Latin American countries. Chinese investors are faced with steep learning curves with respect to local practices (Kotschwar *et al.*, 2012). Often these investors need new skills (e.g. communication, managerial) and improved knowledge and understanding of the contexts in which they are operating. This includes knowledge of standards, regulatory context (e.g. a decentralised government in Peru), and cultural context.

Sustainability standards have been shown to play a role in countries where the current legislation is relatively strong and is enforced, as in Brazil and Chile. Multinational corporations in Chile and Brazil are heavily scrutinised by governments and by civil society groups. In Brazil especially, environmental laws are strongly enforced. This then also applies to Chinese investors and mining operations. One observed trend is that where Chinese SOEs are the main investors *and* are partnering with well-established local companies, the sustainability agendas of mining projects are more rigorous and substantive than when Chinese companies operate alone or take a majority stake – based on the local legislation as a minimum and complemented by local and international sustainability standards.

In joint mining ventures between Chinese and Chilean or Brazilian companies, compliance with national and local legislation is usually high, particularly in the case of large corporations that tend to be more heavily scrutinised by civil society and government. Codelco (Chile) has an agreement for assured supply for 15 years from Codelco's Gaby mine, with Minmetals (China). It implements the same sustainability standards and policies across its projects, regardless of the end market (Codelco sells to China, Europe and North America) (Codelco, 2012). Codelco has its own corporate social responsibility and sustainability initiatives,<sup>19</sup> coupled with international standards such as the Global Reporting Initiative (GRI) and the ISO 14001 standard on Environmental Management. It utilises the ISO 26000 global guidance on social responsibility as well as the guidance provided by the global compact and the World Business Council for Sustainable Development (WBCSD) (Codelco, 2012).

In fact the Chinese government has given explicit backing to ISO 26000 – despite its initial caution towards international standards – having been part of the lengthy multi-stakeholder process in which the content of the standard was negotiated. According to Wang (2011, in Henriques, 2012), China will not only have published its translation of ISO 26000 in 2012, but will begin development of a family of social responsibility standards that may be expected to show considerable influence by ISO 26000. However, more recent research by IIED suggests that there is a lack of agreement between the ministries on whether this standard

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19. The social and environmental impacts of Codelco's own policies and the impact of these other 'external' standards is not immediately clear, and is outside the scope of this paper.

should be developed in China.<sup>20</sup> Anecdotal evidence suggests that some companies in China are using ISO 26000 as a framework for their CSR reports (*China Business*, 2011), for example, CHALCO – Aluminium Corporation of China Limited (the SOE, CHINALCO, is the controlling shareholder of CHALCO). One interviewee from an NGO based in China, who has been involved in supporting SMEs in China to utilise ISO 26000, suggests that the standard is being used *only* as a framework for writing CSR reports, rather than in a more substantive way to guide companies' approach to social responsibility (IIED interview, 2012).

The situation is slightly different in Peru from Brazil and Chile. Institutional weaknesses (such as a weak environment ministry and overlaps in responsibilities between ministries), weak enforcement of legislation and an emphasis on attracting investment regardless of the 'quality' of this investment, has meant lower environmental and social standards being applied in Chinese operations in Peru (as well as arguably in Peruvian operations in Peru). The Extractive Industries Transparency Initiative (EITI) standard (Box 2) has been applied in Peru very recently (EITI, 2012).<sup>21</sup> But China itself has rejected the EITI (Kotschwar *et al.*, 2012). An expert on Chinese mining in Peru, from Universidad del Pacifico in Peru, suggests that Chinese stakeholders do not attend EITI meetings in Peru (IIED interview, 2012). However, Chinese stakeholders do have to disclose payments where they are operating in a country that is EITI compliant, e.g. Peru.

EITI-compliant countries can decide to use either the aggregated or disaggregated reporting standard (Ghana, Liberia, Guinea and Norway, for example, use disaggregated reporting). The current aggregated way in which mining payments are disclosed in Peru means, however, that it is not possible for outside observers to analyse how much individual companies pay (Kotschwar *et al.*, 2012). Disaggregated reporting would increase transparency and would allow relevant stakeholders to identify how much Chinese investors were paying, and allow a comparison to made with other investors (Kotschwar *et al.*, 2012).

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20. This insight is based on the discussions held in a workshop in Beijing about international standards and certification in June 2012, at which a number of government representatives were present.

21. Brazil and Chile are not as yet involved in EITI and are neither compliant or candidate countries. See: <http://eiti.org/countries>.

BOX 2: SUMMARY OF THE  
EXTRACTIVE INDUSTRIES  
TRANSPARENCY INITIATIVE

The EITI seeks to set a global standard for transparency in oil, gas and mining. The EITI is a voluntary coalition of governments, companies, civil society groups, investors and international organisations. Signatory governments are required to declare the revenues they receive from companies, and the companies operating in those countries are required to declare what they pay.

The EITI is designed to provide benefits for: implementing countries (boosting transparency and promoting good governance, so giving clear signals to investors and International Finance Institutions); companies and investors (mitigating political and reputational risks); and civil society (improving transparency).

The EITI has a number of principles and indicators, as quoted here.

- We share a belief that the prudent use of natural resource wealth should be an important engine for sustainable economic growth that contributes to sustainable development and poverty reduction, but if not managed properly, can create negative economic and social impacts.
- We affirm that management of natural resource wealth for the benefit of a country's citizens is in the domain of sovereign governments to be exercised in the interests of their national development.
- We recognise that the benefits of resource extraction occur as revenue streams over many years and can be highly price dependent.
- We recognise that a public understanding of government revenues and expenditure over time could help public debate and inform choice of appropriate and realistic options for sustainable development.
- We underline the importance of transparency by governments and companies in the extractive industries and the need to enhance public financial management and accountability.
- We recognise that achievement of greater transparency must be set in the context of respect for contracts and laws.
- We recognise the enhanced environment for domestic and foreign direct investment that financial transparency may bring.
- We believe in the principle and practice of accountability by government to all citizens for the stewardship of revenue streams and public expenditure.
- We are committed to encouraging high standards of transparency and accountability in public life, government operations and in business.

- We believe that a broadly consistent and workable approach to the disclosure of payments and revenues is required, which is simple to undertake and to use.
- We believe that payments' disclosure in a given country should involve all extractive industry companies operating in that country.
- In seeking solutions, we believe that all stakeholders have important and relevant contributions to make – including governments and their agencies, extractive industry companies, service companies, multilateral organisations, financial organisations, investors, and non-governmental organisations.

Countries can either be 'Complaint' or 'Candidate' depending on their verification and implementation status. To become a Candidate, a country must achieve five sign-up indicators. Once these have been met, EITI implementation involves a whole range of activities to strengthen natural resource transparency, detailed in a workplan. This workplan is discussed with and agreed by stakeholders. To achieve compliance full EITI Validation must take place within 2.5 years. Compliant members are subject to validation at least once every five years, or if the EITI International board requests it. Assessment of compliance is independent. For full details of the EITI rules see: [http://eiti.org/files/2011-11-01\\_2011\\_EITI\\_RULES.pdf](http://eiti.org/files/2011-11-01_2011_EITI_RULES.pdf)

### **Market coverage**

Participation in EITI has grown significantly over recent years: 37 countries have now signed up; 20 are Compliant. See <http://eiti.org/countries> for a complete list of Compliant Countries.

### **Background information**

The Extractive Industries Transparency Initiative was introduced by Tony Blair in October 2002 at the World Summit for Sustainable Development in Johannesburg. The first conference to launch the Initiative was held in London, 2003. The secretariat for EITI was opened in Oslo, 2007. A global conference is held every two years, with meetings of the board held between conferences. The board is made up of 20 representatives from all stakeholders: implementing countries, supporting countries, civil society organisations and business. There is an elected independent Chair – currently Clare Short, former UK Secretary of State for International Development.

### **Funding**

The EITI raises around US\$3 million a year to support its activities. This is funded by various partners: private sector (40 per cent), supporting countries (37 per cent), Norway (20 per cent), NGOs (3 per cent).

Source: Shaping Sustainable Markets, 2013

### 4.3 SUSTAINABILITY STANDARDS IN FORESTRY

The forestry sector in Latin America appears to be the most developed sector in terms of the application of sustainability standards – particularly in countries such as Brazil and Chile where current forest laws are strict and heavily enforced. This has been partly attributed to the demand of European and North American end markets, which has driven changes across the board. Indeed, China's role in the forestry trade is that of processor and manufacturer rather than an end market, although its domestic consumption of final wood products has been increasing (Xiufang and Canby, 2011).

China is now the most significant player in the world trade of wood products – being the world's largest exporter of value-added wood products (e.g. wood flooring and furniture) and one of the largest importers of unprocessed or semi-processed wood (logs and lumber) – partly because there is a limited supply of domestic timber due to China's logging ban<sup>22</sup> (Ganguly and Eastin, 2011). China relies heavily on imports to feed its large trade in wood-related products. It imports over 50 per cent of its forest products, half of which ends up in the EU, US and Japan. These markets increasingly require verification

that the timber comes from legal sources and have increased their environmental and social requirements (Xiufang and Canby, 2011).<sup>23</sup> The amendment to the US Lacey Act (2008), and the EU timber regulation (2010), both of which require all timber to come from legal sources, are also driving changes in the industry in China. A credible certification is one way in which traceability and legality can be assured, and due diligence and 'due care' can be demonstrated.

Very few forest products are exported from China to Latin America but Chile and Brazil are large suppliers of wood pulp to China (ranked 3rd and 1st respectively in terms of volumes of wood pulp imports in 2011) and Brazil also exports logs and plywood to China. Brazil is the biggest exporter of pulp and paper products in Latin America. In 2010, 33.1 per cent of the pulp exports from Brazil went to China (Bracelipa, 2011). China is Peru's biggest timber importer (Putzel, 2009). This trend is likely to continue as the ability of Chinese timber plantations to meet China's aims for quality and production levels has been questioned.

Encouraging increased production from the numerous small-scale producers, and low-income forest owners in China is argued to be vital to guarantee future domestic supply (Xiufang and Canby, 2011).

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22. The Chinese government has attached great importance to domestic afforestation/reforestation programmes in the past decades. The central government has spent 233.2 billion yuan (more than US\$31 billion) on the 415 million mu (27.7 million hectares) of newly planted forests planted between 1999 and 2009. A third of these lands were farmlands returned to woodlands. This effort will continue – the State Forestry Administration has announced that China's government will earmark a total of another 200 billion yuan (US\$30 billion) to afforestation schemes to the end of 2021. Such programmes are also considered part of China's commitment to address climate change (Xiufang and Canby, 2011).

23. There has been some shift of China's forest products trade towards the Middle East and Central Asia as they are less demanding than EU and US markets – but the latter still dominate the market (Xiufang and Canby, 2011).



Any efforts to improve the sustainability of forestry and forest trade in China should include rather than exclude these smaller players. For the pulp and paper industry in China:

*despite shutdowns of small industry players in the 2000s due to negative environmental impacts (particularly water pollution discharge) and poor energy efficiency, the paper industry remains relatively fragmented with the top five players accounting for 18% of total market share in 2008, and the rest producing less than 78,000 tonnes per year. (Xiufang and Canby, 2011: 29)*

There is already evidence that smaller producers are getting forced out of the market, partly due to the implementation of standards. Closure of small and medium-sized mills is attributed to the economic downturn of 2008 and possibly the inability of these smaller enterprises to comply with the requirements of the 'big box' retailers such as WalMart and IKEA (Xiufang and Canby, 2011). So while multinationals may be driving use of standards, this process is likely to reinforce consolidation of the industry and lead to the exclusion of smaller players. However, an FSC representative argues that the majority of the 2500 FSC chain-of-custody certificates in China are held by SMEs (IIED interview, 2012).

### **Chinese national and overseas forestry standards**

The State Forestry Administration (SFA) and the Ministry of Commerce (MOFCOM) created and published a guide on Sustainable Overseas Forest Management and Utilization by Chinese Enterprises in 2009 to signal China's commitment 'to the protection, restoration and sustainable development of global forest resources'. The standard was drafted by the Forestry Project Planning and Designing Institute of the SFA

Forest Product Industry Planning and Designing Academy, in collaboration with the World Wildlife Fund (WWF), Nature Conservancy (TNC), International Union for Conservation of Nature and Natural Resources (IUCN), and Forest Trends (SFA, 2009). The guidelines are explicitly recognised as a tool to help implement China's 'going global' strategy (SFA, 2009) that 'will be gradually embraced'. The original impetus for creating the guidelines came from the Chinese NGO, the Global Environment Institute, which was also involved in drafting the guidelines.

The guidelines aim to provide the industry with 'management criterion and a *self-discipline basis* for the management and utilization activities of overseas forest resources by Chinese enterprises' (emphasis added) (SFA, 2009: 12). The guidelines' emphasis is on legality and meeting existing obligations and regulations (both in the host country and according to international agreements that China has signed up to).

The guidelines have a series of basic principles (SFA, 2009):

1. respecting national sovereignty of the host country
2. mutually beneficial cooperation (Chinese enterprises making positive efforts to promote local economic and community development)
3. integrating ecological, economic and social benefits
4. combining government guidance with industry self-discipline
5. sustainable management and utilisation of forests
6. resource saving (of forest, land and energy resources).

## FOUR STANDARDS TO IMPROVE THE SUSTAINABILITY OF CHINA-LATIN AMERICA TRADE AND INVESTMENT CONTINUED

The guidelines then offer specific guidance on laws and regulations, management and utilisation of forest resources, ecological protection and community development. For community development, for example, the guidelines suggest that:

*when conducting the activities related to the forest management and utilisation, the enterprises concerned shall give full consideration to the interests of local residents and take appropriate measures to prevent the said activities from directly or indirectly infringing, threatening or undermining the ownership or right of use of local residents toward legal resources. (SFA, 2009: 25)*

SFA, cooperating with WWF and other NGOs and research institutions, has been promoting the guidelines in Russia, Gabon, Guyana, and Papua New Guinea (chosen because of the known presence of Chinese forestry companies). It has conducted demonstrations in nine Chinese overseas timber companies (both SOEs and private companies). Ten Chinese companies made commitments to follow the guideline in 2011 (IIED interview, 2012). The SFA has attended a number of trade shows and international events to promote the use of the guidelines, with private-sector 'pioneers' showcasing their experiences of implementing the guidelines.

Nevertheless some aspects of the guidelines are quite vague, for example recommending that companies ensure 'endangered flora and fauna are marked on a map' and that 'corresponding measures' are formulated, as well as measures for the protection of 'typical ecosystems'. The guidelines are therefore open to a significant degree of interpretation and do not offer much in the way of tangible practical guidance. Is it unclear if and how 'compliance' with, or

implementation of the guidelines are monitored. Their voluntary nature and the emphasis on self-discipline presumably means there is no scope for the implementation of the guidelines to be enforced. A representative from IUCN explained that the guidelines are quite general, in that they are designed to apply to any overseas context in which a Chinese company is operating (IIED interview, 2012). This lack of specificity can be a barrier for companies operating in contexts with particular challenges that the company needs to understand – the guidelines cannot offer this kind of specific guidance.

The IUCN representative also explained that the main challenges around implementation of the guidelines are technical capacity and support for companies to apply the guidelines in particular contexts, and motivation. She observed that the motivations for large companies and SMEs to implement the guidelines are very different – SMEs will find it harder to implement the guidelines and cannot necessarily afford the costs of doing so. NGOs and the SFA have an important role to play in supporting SMEs to implement the guidelines. Companies who are selling or looking to sell to EU and US markets are more likely to implement the standards than those selling to other countries. Nevertheless, it is unclear to what extent the EU and US markets recognise the guidelines as a reputable and rigorous verification of the sustainability of timber and forestry operations/companies. Credibility, recognition (and market-driven or government demand) are likely to be important determinants in future use of the guidelines.

A representative from the Chinese Academy of Forestry explained that there is a gap between what is stated in the guidelines and the practice of companies implementing the guidelines as part of the pilot (IIED interview, 2012). This

representative argued that capacity building is required for companies:

*the extent to which the guide will be implemented in the future depends on if the government will have more rigorous policies. So far it is not compulsory but nor have other countries made this kind of guide compulsory. But the standard should also be market-led, and businesses should want to apply the guidelines for business gains related to being more sustainable.*

The SFA is recommending that the 'Green Credit' checks (for example by Chinese banks) use the guidelines as a reference point for their lending decisions (IIED interview, 2012).

An IUCN representative has explained that national associations (such China's National Forest Products Industry Association) have an important role to play in encouraging their members to implement the guidelines. As yet, they are not explicitly promoting the implementation of the guidelines. There are political challenges, with a gap between the desires and priorities of the SFA and the Ministry of Commerce, concerning which organisation should be the main driver of implementation of the guidelines.

China has developed its own national voluntary standard for forestry – China's National Forest Certification Program for timber and forest products. This is administered by China's Forest Certification Council (CFCC). It includes both a chain of custody and forest management standard. It has 9 principles, 45 criteria and 118

indicators.<sup>24</sup> According to Xu Bin from the Chinese Academy of Forestry (IIED interview, 2012), who was a key drafter of the standard, the FSC was heavily referenced during drafting of the CFCC standard.

Forests are to be certified against the standard by a third party certification body. According to Xu Bin, certifiers are first recommended by the local forest bureau, they are then 'qualified' or accredited by CNCA (China's National Certification and Accreditation Administration). To date, only one institute has qualified to be a certifier of CFCC, the Zhonglin Tianhe Beijing Forest Certification Center (ZTFC<sup>25</sup>). Its licence is due to expire at the end of December, 2016. According to Xu Bin, six or seven institutes are currently applying to be certifiers of the standard.

According to ZTFC (in July 2012), 10 forest management companies (accounting for a forested area of around 1million hectares in total) and two forestry-product processing companies have finished the main assessment for the certification. Of these, eight of the forest management companies and the two processing companies have been certified by CFCC. Those companies include leading SOEs and large private companies, for example Asia Pulp and Paper. Some multinationals have also demonstrated interest in the standard (ZTFC, 2012). In 2010, ZTFC signed a Memorandum of Understanding with Walmart (China) and Walmart Global's sourcing department (referred

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24. The principles relate to: 1) National legal framework 2) Forest tenure 3) Local community and labourers' rights, 4) Forest management plan 5) Silviculture, 6) Biodiversity conservation, 7) Environmental impacts, 8) Forest protection, and 9) Forest monitoring. See <http://www.cfcs.org.cn/file/fileup/%E6%A3%AE%E6%9E%97%E7%BB%8F%E8%90%A5%E8%AE%A4%E8%AF%81%E6%A0%87%E5%87%86%E8%8B%B1%E6%96%87080109-Eng.pdf> for more information.

25. See <http://cfcc-ztfc.com>

## FOUR STANDARDS TO IMPROVE THE SUSTAINABILITY OF CHINA–LATIN AMERICA TRADE AND INVESTMENT CONTINUED

to as an ‘environmental sustainable development cooperation agreement’) to jointly promote ‘worldwide environmental sustainability activities and practices, including forest certification’ (Walmart, 2012: 1). Though CFCC is not mentioned explicitly, the parties involved could suggest that Walmart will be a buyer of CFCC certified timber when it becomes available. As part of the agreement, all parties involved will ‘provide technical consulting and professional trainings on forest certification for forest certification assessors, suppliers, managers of forest-related businesses and agencies to be certified’ (Walmart, 2012: 1).

Once a certificate is issued, it will last for five years, although checks take place every year. If ‘anything is found to be seriously wrong, the certificate will be cancelled’ (Xu Bin, IIED interview, 2012). Some forestry experts have argued, based on the certification pilots, that the standard ‘has not been implemented well’ or rather that the standard’s requirements are not particularly strict – hence the standard having not yet been officially recognised by PEFC. According to one interviewee who is an expert in the forestry industry (but wishes to remain anonymous), certification trials have taken place and revealed that certification was relatively easy to achieve – raising some concerns over rigour. However, the pilot phase is designed to test the content of the standard and forest managers’ ability to implement it, and changes to the content of the standard may be made subsequently.

Some parties have expressed concern about the independence of the standard and its certification process – and therefore its credibility – since the State Forestry Administration is responsible for both the standard and certification (with the ex-head of the SFA having a stake in the certifier). Credibility may be an issue because the standard

is not strictly third-party certified. ZTFC, the only certifier currently in operation, ‘comes under the SFA’ (Walmart, 2012) and is owned by the ex-head of the SFA. The SFA is likely to be keen to see as many forestry operations certified as possible.

According to Xu Bin from the Chinese Academy of Forestry (IIED interview, 2012), there are a number of drivers for the creation and implementation of CFCC. These include access to international markets (because domestic demand and consumption of certified timber remains limited), and an anticipation that government procurement policies and policies more broadly will demonstrate a preference for certified timber.

CFCC has recently joined the Programme for the Endorsement of Forest Certification (PEFC), though has not yet been endorsed by it. The intention is that joining PEFC will help the CFCC work towards international recognition of the scheme and endorsement by and harmonisation with PEFC ([Pulpandpaperworld.com](http://Pulpandpaperworld.com), 2012). CFCC will have to meet PEFC’s principles of Sustainable Forest Management. Harmonisation was sought with PEFC, rather than FSC. This is despite there being a significant area of land already under FSC-certified sustainable forest management – and a greater number of processors and manufacturers having obtained FSC chain-of-custody certificates than PEFC equivalents (see below).

PEFC’s model is different from FSC’s in that it is a framework for mutual recognition of national standards (participating national standards have to meet PEFC’s sustainability benchmarks). FSC on the other hand has its own standards, criteria certification and process which countries have to implement, though appropriate indicators for the principles and criteria are created for

particular countries (e.g. China), through in-country multi-stakeholder processes. This offers some flexibility in terms of adapting the standard for local circumstances. Once these are met, the national standard can be FSC and labelled as such. For PEFC, accreditation can be carried out by national accreditation bodies, unlike FSC. With PEFC the national scheme can maintain its own name and label should it wish, though it can also use the PEFC logo. PEFC currently has no forest coverage in China because the national standard has not yet been finalised and met the benchmarks of PEFC. However, there are 99 wood-product manufacturers in China who are certified under the PEFC-Chain of Custody programme in China (Ganguly and Eastin, 2011).

It is also argued that FSC follows a stricter set of guidelines that allow for less country-specific flexibility (Ganguly and Eastin, 2011), which may have been an issue for China.

*there have been strong disagreements between FSC and the Chinese government regarding the certification criteria [sic] included in the Chinese certification program... related to the social and indigenous people's rights aspects of the Chinese National Forest Certification (CNFC) program. (Ganguly and Eastin, 2011: 6)*

However, a representative from FSC has explained that communication and dialogue continues between FSC and the CFCC and that, despite CFCC's intention of working towards harmonisation with PEFC, 'it is hoped that FSC and CFCC can be as compatible as possible' (IIED interview, 2012).

A representative from China's National Forest Products Industry Association (CNFPIA) sees the key benefits for companies who get CFCC certified as 'increased market access and customs clearance.' He explains that 'the majority of large timber companies in China implement FSC, but the vast majority of smaller companies do not and are accused of water pollution and resource wastage' (IIED interview, 2012). Ganguly and Eastin (2011) also argue that a growing number of Chinese timber and timber-processing companies, including major hardwood-flooring manufacturers, are obtaining forest management and chain-of-custody (CoC) certifications from FSC-approved certifiers. Between 2000 and 2010, the number of

companies in China that have obtained FSC CoC certification jumped from 12 to 1562 (Ganguly and Eastin, 2011). By 2013, this had risen to 2412 companies (FSC, 2013). Despite this positive trend, this accounts for only a very small proportion of all wood-manufacturing firms in China (less than 4 per cent) and 'only a small fraction of the wood products manufactured by these CoC certified firms use certified wood' (Ganguly and Eastin, 2011).

A total area of 2.59 million hectares has been certified under the FSC's forest management programme in China (FSC, 2013) (Table 1). Most of the certified forest area is within state-owned forests and many are integrated with state-owned wood-manufacturing operations that have also received CoC certification (Ganguly and Eastin, 2011). The lack of availability of FSC-certified wood, from both domestic and international sources, has been cited as the major reason why such a low percentage of manufactured wood products are produced from certified wood in China – 'the adoption of FSC Forest Management certification in China has been slower than CoC certification, primarily due to the fact that virtually all forests in China are state-owned' (Ganguly and Eastin, 2011: 5).

A representative from FSC (IIED interview, 2012) explains that are specific challenges to scaling-up FSC (and certification in general) in China and in determining whether CFCC seeks harmonisation with FSC or PEFC. These include the 'political challenges' in getting state-owned forests certified and the choice that needs to be made 'between international and local schemes' as well as the quotas for timber production. He argues that the State Forestry Administration is not particularly market-driven, which can be a challenge for the up-scaling of FSC – despite the fact the scheme that has captured more of the market in China (and the market in other demand and supply countries of FSC) than any other forestry certification scheme.

The FSC representative explains that multinationals in China (such as IKEA and Walmart) have been significant in driving the growth in FSC certification, though they have struggled with challenges of side-selling of certified produce (i.e. selling to other buyers than those agreed upon) and a lack of supply due to quotas. Demand for LEED-certified buildings<sup>26</sup> has also played a role in driving demand for FSC.

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26. LEED certification is a recognised standard for measuring building sustainability. See: <http://www.usgbc.org/leed>

FOUR  
STANDARDS TO IMPROVE THE SUSTAINABILITY OF  
CHINA-LATIN AMERICA TRADE AND INVESTMENT  
CONTINUED

TABLE 1: MARKET COVERAGE OF CERTIFICATION SCHEMES IN CHINA, 2013

INTERNATIONAL	FOREST COVERAGE (MILLION HECTARES)	CHAIN-OF-CUSTODY CERTIFICATES
FSC	2.59	2412
PEFC	0 (dependent on a national scheme being established in China)	99
NATIONAL		
CFCC	1.0 (estimated, not third-party data)	2 (estimated, not third-party data)

There are a number of challenges for small forest managers who wish to achieve FSC certification in China. An FSC representative explains that issues remain around land tenure in China and that some historical tensions have not been resolved. FSC will not certify plantations created through conversion of natural forest since 1994, nor genetically modified trees, and these can be challenges for small forest operators. Small operators have also been struggling with having the appropriate management capacity to meet the needs of the FSC standard, although FSC is now implementing specific standards for small operators and organising training sessions for forest managers and certifiers to help more smallholders get certified. Small operators tend to need to be well-organised and already have a market link – through which these operators may obtain co-investment and support. Donors can play a role in supporting operators but a market needs to be identified to ensure there is demand. FSC explains the importance of maintaining credibility of the FSC standard, particularly in

China, through international auditors auditing the external certifiers and by having a complaints mechanism in place so anyone can raise suspicions of non-compliance anonymously.

Each industry in China has an Association – these are not-for-profit organisations that help to manage a particular market (e.g. timber) and establish standards therein. The China Timber Circulation Association has a membership of 600 timber enterprises. These members can apply for a credit rating, verified by the Association, which is a type of quality assurance; the highest rating is AAA, which 10 companies achieved in 2010. The idea is that consumers can then choose the ‘best’ company. The rating system has nine components, one of which is related to corporate social responsibility (e.g. the achievement of ISO 14001, whether the timber comes from certified sources, and whether the enterprise contributes to afforestation, environmental conservation or sustainable forests).

However, these associations are typically linked to government in some way and in some instances are actually established by the government – this is different from associations in other countries like Brazil, which are independent and play an important role in lobbying government on the needs and interests of businesses. In some cases, associations may be 'consulted' on new policies, but in reality consultation is not meaningful and the associations are regarded as a key vehicle for reinforcing and promoting government policies. One Chinese expert who has worked with and studied forestry industry associations around the world has explained that the lack of independence among industry associations is a key barrier to more dynamic industry growth and can work against the views of SMEs who lack a proper channel for feedback to government (IIED interview, 2012).

### **International and national standards in forestry in Chile, Peru and Brazil**

In addition to the international certification scheme of the Forest Stewardship Council (FSC), Brazil also has a national scheme: *Certificação Florestal* (Cerflor), also voluntary. Cerflor has been operational since 2003 and is endorsed by the Programme for the Endorsement of Forest Certification Schemes (PEFC), which means that it complies with PEFC's sustainability benchmarks (PEFC, 2012a). PEFC is the world's largest forestry certification system by hectares. Cerflor follows Brazilian legislation as well as international conventions recognised by the government<sup>27</sup> and is a product of the joint effort of

stakeholders – NGOs, producers, governments, consumers, universities and research institutions (PEFC, 2012a). Of the total 519 million hectares of forest in Brazil (FAO, 2010), 7.36 million hectares are FSC certified (FSC, 2013) (approximately 1.4 per cent of total forest coverage, based on 2010 figures for forest coverage). The total Cerflor certified area is 1.26 million hectares (Inmetro, 2012), or 0.24 per cent of total forest coverage.

In Chile, forestry exports (mainly pulp) reached US\$5177 million in value in 2011 and went mainly to China and APEC countries followed by the European Union, other Latin American countries and the USA (ODEPA, 2012b). The certification schemes used in Chile include FSC and CERTFOR Chile. CERTFOR is the Chilean national certification system internationally endorsed by PEFC since 2004 (PEFC, 2010b). CERTFOR includes four certification standards (sustainable forest management (SFM) for plantations, SFM standard for native forests, chain of custody standard and group certification standard) and is the main certification system in Chile (PEFC, 2010b). As of 2010, 82 per cent (1,911,920 million hectares) of forestry plantations in Chile was CERTFOR-certified (PEFC, 2012b). In April 2013, 1.17 million hectares in Chile were FSC-certified (FSC, 2013).

In Peru, 959,722 hectares of forest are FSC-certified (FSC, 2013) (1.4 per cent of the total forested area in Peru – 68,742,000 hectares) (Mongabay, 2012). But historically there have been issues with illegal logging and timber trade

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27. International conventions and processes recognised and applied by the Brazilian government include the Convention on Biological Diversity, the Convention on International Trade in Endangered Species of Wild Fauna and Flora, the Kyoto Protocol, the Biosafety Protocol and the International Tropical Timber Organization (PEFC, 2012a).

due to weak implementation and enforcement of the law. In recent years, changes to and enforcement of the Peruvian Forest Law (passed in 2000) have helped to drive some improvements in sustainability of the forestry sector (Putzel, 2009). This was arguably driven by demands of the US market, because of the significant scale of illegal or 'informal' logging in Amazonia (which reached up to 88 per cent between 2002 and 2006, according to Putzel (2009)). A condition of the US–Peru Free Trade Agreement (in effect since 2009) was the modification and increased enforcement of the Peruvian Forest Law in order to fulfil the requirement of the US Lacey Act and Europe's FLEGT licensing scheme,<sup>28</sup> which ban commerce in illegally sourced timber and timber products (Putzel, 2009).

Though data exist on the extent/market coverage of sustainable forestry certification in Chile, Brazil and Peru, it is unclear what percentage of certified timber from these countries is actually being exported to China. Anecdotal evidence suggests that at present the main markets for certified timber remain European and North American (Muthoo, 2009). There is therefore a dual system depending on end market – with little or no certification for domestic markets or for markets that are as yet 'non-sensitive' to sustainability requirements (typically in developing countries).

## 4.4 SUSTAINABILITY STANDARDS IN AGRICULTURE

### International and national standards in Latin America

Soy is the most significant product in Chinese–Latin American trade in agriculture. There are two high-profile mechanisms that have been applied to the global soy trade: the Soy Moratorium and the Round Table on Responsible Soy (RTRS) (Box 3). Attempts are being made to introduce the RTRS certificate to soy production in South America. National interpretations of the standard have been completed for Argentina, Brazil and Uruguay and in June 2011 the first South American producers were RTRS-certified. National interpretations for India, Paraguay, China and Bolivia are in progress. However, in a strategic analysis for the production of responsible soy in Brazil and Argentina carried out by the Instituto de Estudo do Comércio e Negociações Internacionais (2011) for the RTRS Association, it is recognised that China, as the largest soy importer in the world, does not demand any of its soy imports to be sustainably produced or certified. The increase in Chinese demand for Brazilian soy (compared to that of the European Union) could therefore entail a reduction in incentives for producers to adopt and implement sustainability standards. This could result in a setback in the current trend of sustainability standards seen in the agribusiness sector in Brazil – and possibly in other countries from which soy is sourced.

28. See <http://ec.europa.eu/environment/forests/flegt.htm>.



### BOX 3: THE ROUND TABLE ON RESPONSIBLE SOY

The Round Table on Responsible Soy (RTRS) is a multi-stakeholder initiative working to certify soy as responsible. Originally, it provided a forum for dialogue between various actors in the soy supply chain and civil society, but in 2010 it drew up standards for certification of soy products and for the supply chain (Chain of Custody). In June 2011, the first farm was RTRS certified. The RTRS has a Certificate Trading Platform, which has facilitated transactions between certified producers and buyers.

The RTRS standard for responsible soy production includes requirements to halt conversion of areas with high conservation value, promote best management practices, ensure fair working conditions, and respect land-tenure claims. The principles behind these production standards are:

- legal compliance and good business practice
- responsible labour conditions
- responsible community relations
- environmental responsibility
- good agricultural practice.

These guiding principles inform the development of 'national interpretations' which are drawn up by a technical working group. So far, Brazil, Argentina and Uruguay have completed national interpretations with India, Paraguay, China and Bolivia in the process of doing so. The technical working group consists of representatives from industry, civil society and producers.

Certification against these principles must be undertaken by independent auditors. It is not clear how regularly monitoring must take place. A set of supply chain standards have also been published, aiming to ensure traceability throughout the supply chain. A number of modules describe the various options available. These include specifications for a mass-balance model and/or a fully segregated model. In addition, there are specifications for non-genetically modified and multi-site supply chains.

#### Market coverage

As of 2012, there were 18 certified producers. In total there was 959,531 tons of certified soy produced on 333,956 hectares. Global production of soybeans in 2011 stood at 251.5 million tons (USDA, see [http://www.soystats.com/2012/page\\_30.htm](http://www.soystats.com/2012/page_30.htm)).

#### Background information

The RTRS originated from the Responsible Soy Forum in London, UK in May 2004. The RTRS was formalised and registered in Zurich in November 2006. Numerous meetings have taken place since then and standards have been developed and piloted since 2009. The first version of the Standard was published in June 2010. Membership of the RTRS is voluntary, multi-stakeholder and grouped according to sector type (number of representatives in brackets): producers (29); industry, finance and trade (72); civil society (16). In addition there are 28 organisations that are 'observers'. Information on funding is not publically available. RTRS-certified status is applicable to all kinds of soybeans including genetically modified produce

Source: Shaping Sustainable Markets, 2012

It has been argued that other strategies, i.e. those that do not involve certification, will be necessary to improve the sustainability of the soy trade in light of the Chinese end market, which is regarded as price sensitive and less concerned with environmental footprints (TNC, 2011). Possible strategies include: focusing on multinationals and the reputational risk associated with deforestation and encouraging them to track their sources of soy and its links to deforestation; providing non-price-premium incentives to producers (such as subsidised credit, access to extension services); and intensifying production on already cleared land (TNC, 2011).

In the agricultural sector in Brazil, Chinese companies have yet to start any major projects, although several have been announced. For example, the China National Agricultural Development Group Corporation (CNADC) will be working with the government of the state of Goias in expansion projects of grain plantations and will invest in the construction of a railroad. The current major exporters to China from Brazil are large multinationals, such as Cargill, ADM and Bunge. These serve Northern markets (i.e. Europe and North America) as well as Southern, and have relatively well-developed sustainability policies, particularly in comparison to non-OECD exporters.

In Chile a number of initiatives involving good agricultural practices have been implemented; this has been attributed to demands for farmers to become GLOBALGAP, EUREGAP or USGAP certified (ChileGAP, 2012). ChileGAP was developed in Chile at the request of the Chilean Association of Exporters and has achieved equivalence with GLOBALGAP (ChileGAP, 2012). There are over 130 companies (farms)

specialised in fruit production that have been certified (ChileGAP, 2012) but information is lacking on how up-to-date this figure is, and on the impact of this voluntary scheme.

Another initiative to help farmers comply with international requirements is that of Fedefruta – the National federation of fruit producers of Chile. This helps farmers to incorporate good agricultural practices into their operations by offering audits and training for EUREPGAP and USAGAP certification (Fedefruta, 2012). These initiatives reflect the impact of European and North American markets on the Chilean fruit market. However, the export of agricultural products from Chile to China is just taking off, and information on the extent of this trade, and whether any standards are being implemented, is scarce. The Chileans are showing significant interest in selling fruit to the Chinese market, as well as meat and wine. There is a China–Chile demonstrative farm in Tianjing near Beijing.

### Chinese national standards

The standards published by the Chinese government for agricultural products are currently focused on food safety and meeting customs requirements such as for cleanliness, packing and product quality (IIED interview, 2012). So far, there are no Chinese standards related explicitly to sustainable production for food imports into China or out of China – though the Chinese Green Food initiative was launched in 1990 by the Ministry for Agriculture for domestic production. It aims to ‘enhance food quality and safety, to promote consumer’s health, and to promote agricultural bio-environment for sustainable development’ (Green Food, 2012). At present, it appears that sustainability standards are not being applied to food imported into China.

However, some of the multinationals operating in China, such as IKEA, are playing a role in driving the market for certification. IKEA, which has stores in China, requires all of its cotton suppliers to be certified under the Better Cotton Initiative

(BCI), regardless of where they are in the world. IKEA has been working with villages in Xinjiang province to support the application and adoption of BCI. This is also the case with certified forest products.

**TABLE 2: SUMMARY OF SUSTAINABILITY STANDARDS/GUIDELINES RELEVANT TO CHINA-LATIN AMERICAN TRADE\***

	CROSS-SECTORAL	MINING	AGRICULTURE	FORESTRY
International standards				
	ISO 26000	EITI Global Compact ISO 14001 GRI	Soy moratorium Round Table on Responsible Soy GLOBALGAP EUREPGAP USGAP Better Cotton Initiative	FSC (PEFC, see below)
National standards				
China	Guidelines on investments overseas (2009) Green credit guidelines (2012) Guidelines on environmental protection for China's outbound investment and cooperation (2013)		Green Food ChinaGAP	CFCC Guide on Sustainable Overseas Forest Management and Utilisation by Chinese Enterprises (2009) PEFC chain of custody
Chile			ChileGAP	CERTFOR (PEFC)
Brazil				Cerflor (PEFC)
Peru		EITI		

\*This table is not exhaustive. It reflects the major sustainability standards mentioned during IIED research.

# FIVE CONCLUDING REMARKS

Trade and investment between Latin America and China is booming, particularly in the natural resource and extractive sectors. This brings with it new challenges and opportunities for the pursuit of sustainable development. The nature of trade and investment between emerging and developing countries – the behaviour of companies, the implementation and development of standards, and overall sustainable development outcomes – are shaped by a number of governance factors. These include:

- the regulatory context in which the trade/ investment takes place
- the regulatory (hard and soft) context from where the investment comes
- the nature of the investment or partnership
- the demands of external investors and shareholders
- the level of activity of civil society (for example NGOs and the extent of press freedom) – related to what the government will tolerate
- the existence of other accountability drivers, such as institutions to provide credible monitoring and to push for transparency and effective reporting (such as EITI, Global Witness, Publish what you Pay).

In this sense, 'good' governance comes from a variety of different directions and sources.

Initial evidence presented in this paper suggests that sustainability considerations are increasingly on the agenda and Chinese companies are making efforts to address the social and environmental impacts of their operations, as well as developing constructive relations with stakeholders. A number of international standards

(including the GRI, ISO 26000, ISO 14001, the Global Compact, and EITI) are being used to meet the demands of investors, consumers and other stakeholders in Chinese–Latin American trade and investment. In some cases, national standards are being developed, such as ChileGAP, CFCC and China's 'Green Banking' guidelines. This is possibly due to a perception of the limitations or inappropriateness of the existing set of international instruments, though there are also attempts to see these national standards achieve equivalence with international standards – presumably to expand market opportunities.

Multinationals can have higher standards overall, driven by requirements from consumers, investors and governments in developed countries. They typically maintain a more consistent approach to standards and sustainability across all of their operations, regardless of country of operation. These actors may play a role in driving broader changes in the market. IKEA, for example, which operates in China, requires all of its suppliers to have achieved FSC certification and to be compliant with the Better Cotton Initiative. IKEA China is having to source half of its timber from European, US and Australian sources because China's awareness and production of FSC-certified timber is low, but IKEA may help to drive certified production in China – as it is with cotton.

Evidence also suggests that European and North American markets are driving adoption of sustainability standards in emerging and developing economies. Chinese companies wishing to target these markets may adopt higher standards, which they then apply to all of their practices. But, often, there is a dual system depending on end market, with no certification for domestic markets.

Unsurprisingly, standards are most likely to be implemented where there is an effective regulatory context. Laws set the minimum standards required, upon which private standards tend to build. In some cases there is a perception that standards are meaningless until the legislation and enforcement is strong enough to establish a bare minimum which companies need to satisfy and can then move beyond. Government support for standards is also important, e.g. the Peruvian government support for EITI. The form of investments (mergers and acquisitions, joint ventures or greenfield) permitted by law in a country, or encouraged by the government, also affects the adoption of standards. For example, where Chinese companies have been able to purchase majority stakes in overseas companies or set up independently (as in the case of Shougang Hierro Peru), there are fewer external pressures and accountability mechanisms to drive the use of standards, or standards are not 'inherited'.

Investors and financial markets play an important role in driving accountability, and can be influential drivers of behaviour change. As Kotschwar *et al.* (2012: 19) explain: 'Investors that have to withstand scrutiny as they register their equity, raise capital, and seek multilateral assistance in international markets tend to adopt defensible standards, or face reputational risk.' Initial evidence suggests that investors within China are beginning to adopt lending practices partly shaped by CSR considerations. Industrial Bank (China) is the first (and currently only) bank in China to have signed up to the Equator Principles (China Dialogue, 2012), despite the Chinese government not officially endorsing the principles. Although the exact driver behind the Industrial

Bank's decision to adopt the Equator Principles is not known, it appears that the International Finance Corporation played a role in encouraging their adoption, and certainly in making 'strategic suggestions and technology support for Industrial Bank to implement the Principles' (China CSR, 2008). The Industrial Bank is regarded as an industry leader in terms of sustainable finance and green banking (China CSR, 2008). These processes are not free from politics – the top three banks in China financing Overseas Direct Investment (China EXIM bank, China Development Bank and Bank of China) have not signed up to the Equator Principles. China's Green Credit guidelines are likely to play a growing role in shaping the nature of Chinese investment both within China and overseas. It will be important to monitor the implementation of these guidelines and their impact.

Civil society – and government's acceptance of civil society activity – plays an important role in holding companies accountable and in highlighting bad practice as well as offering or withholding a 'social licence' to operate. In Peru, a social licence to operate is enshrined in law. Kotschwar *et al.* (2012) argue that 'supporting groups that monitor the activity of corporations helps to shed light on both positive and negative practices and helps encourage constructive behaviour'.

Indeed, standards and guidelines ultimately work well only in circumstances where someone can be held accountable and where there is third-party auditing and transparency. Investors, for example, may ask questions about environmental and social standards before financing a project, or stakeholders may raise complaints with investors if problems arise. This is more challenging in the

case of Chinese SOEs, which can be less transparent to external stakeholders and/or do not necessarily have a variety of stakeholders involved (e.g. independent/third-party investors). They can therefore be subject to fewer accountability drivers/mechanisms in comparison with private Chinese companies (Sanborn, 2012).

Increasingly, Chinese SOEs and private companies are being exposed (either externally by market demands or internally by government policy) to sustainability requirements and standards. According to Kotschwar *et al.* (2012), domestic environmental standards have begun to become more stringent since the mid-2000s, and the Chinese government has pushed for companies investing abroad to pay attention to environmental and social factors as well as profit (as part of its 'green development' strategy; see WWF, 2012). Loosely defined corporate social responsibility requirements have been put forth (Kotschwar *et al.*, 2012). In addition, 'Chinese' standards are growing in relevance and use (e.g. CFCC, Green Credit guidelines, ChinaGAP) and China's 'going global' strategy explicitly recognises the importance of meeting international standards. Indeed, as well as developing its own standards, China is also looking to achieve equivalence and harmonisation with existing international standards (e.g. PEFC, GLOBALGAP) that best suit the Chinese context – for example a choice of PEFC over FSC.

This trend is also reflected in a growing emphasis in China on sustainability reporting. For example, at least 60 major Chinese companies use the international Global Reporting Initiative guidelines, with the state-owned China Overseas Shipping Company securing the GRI's most stringent 'A+'

level rating for its sustainability report (Zadek, 2012). Zadek argues that China's growing emphasis on corporate social responsibility is not simply 'greenwash' (though examples of this exist – as they do with companies in the North), but part of a strategic move to become the world's leading green and inclusive economy. The rise of sustainability reporting in China has been attributed to the State-owned Assets Supervision and Administrative Commission (SASAC) requiring all state-owned enterprises to publish CSR reports by 2012. By 2010, state-owned enterprises accounted for 78 per cent of all companies releasing these reports (BSR, 2012).

This paper aims only to stimulate discussion, and a number of significant research gaps remain. Improved understanding of the role of Chinese SOEs – and their adoption of standards – in overseas investment and trade is clearly important because of their size and dominance and their regular role as first movers. From a development perspective, however, it is particularly important to understand the role of Chinese and Latin American SMEs in this trade and investment, and the potential for the development and application of standards to be inclusive or exclusive of SMEs.

The role of the informal economy in this international trade is also important. Peru is the sixth-largest informal economy in the world (Peru21.pe, 2013). In China, for example, the agrifood market is dominated by a large number of small farmers, traders and wholesalers, and the informal economy at the farm level continues to dominate with little penetration from the modern market (Jia and Huang, 2011). Initial evidence suggests that the application of standards in these countries could lead to exclusion of smaller

players (see, for example, Mo *et al.*, 2012 on the impacts of government attempts to standardise the dairy industry in China). Understanding how to include these players meaningfully in efforts towards sustainability (and food safety) will be vital. Understanding how to ensure that China and Latin America's transition to sustainability is both green and inclusive is an important area of further research.

A number of questions warrant further attention:

- What are the attitudes of Chinese companies and SOEs to certification, and how much of this is influenced by re-export and how much by domestic drivers?
- What are the behaviour and attitudes of SMEs involved in China–Latin American trade towards sustainability and standards?
- How effective are the tools being developing within China and other emerging and developing countries and what impact are they having?
- What sort of tools would be most appropriate for a Latin America–China trade axis to drive sustainable trade and investment, compared to existing international standards, and how can these be inclusive, rather than exclusive of small-scale producers and SMEs?
- How will international standards bodies make changes to their codes and standards, and bring in Southern business stakes?

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## APPENDIX 1: LIST OF INTERVIEWEES

This series of interviews was carried out especially for this report. When cited in the text, these are referred to as 'IIED interview, 2012'.

### Companies

- Forest sector (pulp). Private company, Chinese. Senior Procurement Manager.
- Cross-sectoral. Multinational retailer with operations in China. Buyer in upholstery.
- Mining (chromium). State-owned enterprise, Chinese. Buyer.
- Mining. State-owned enterprise, Chinese. Manager of Integrated Business Department.
- Mining. State-owned enterprise, Chinese. Supply Chain Manager (cement).
- Mining. Private company, Singaporean with Chinese subsidiaries. Managing Director.
- Construction (in relation to building materials, i.e. timber). State-owned Enterprise. Flooring Department.

### Ministries/government organisations

- Ministry of Agriculture, China.
- State Forestry Administration, China.

### Associations

- US Grain Councils, American Soybean Association.
- China Non-ferrous Metals Standards Metrology and Quality Institute.
- China National Forest Products Industry Association (CNFPPIA).
- Brazil Mining Association (IBRAM), Environmental Manager.
- China-Brazil Business Council (CBBC).

- Brazilian Rural Society (SRB), Advisor to SRB's President.

### Academics and NGOs

- Xu Bin, Chinese Academy of Forestry.
- Dr Alvaro Comin, Lecturer at King's College London. Dr Comin is an expert in Labour and Development Studies in Brazil, having worked in the area for over ten years.
- Dr Cynthia Sanborn, Director of the Research Centre at the Universidad del Pacifico (CIUP), Peru.
- Julia Cuadros, Deputy Director, Cooperacion, a Peruvian NGO that focuses on promoting sustainable development in areas with high levels of natural resources exploitation such as mining and fishing.
- Ruben Gonzales-Vicente. PhD candidate, University of Cambridge. Research focusing on the internationalisation of China's mining industries and the Chinese state, as well as the developmental impact of Chinese mining investment in South America (see <http://www.geog.cam.ac.uk/people/gonzalez-vicente/>).
- WWF China.
- IUCN.
- Ecologia.
- A Chinese national who has worked with and studied industry associations (especially the forest industry) around the world.

### Certifiers

- Forestry Stewardship Council.





# SUSTAINABILITY STANDARDS IN CHINA–LATIN AMERICA TRADE AND INVESTMENT

## A DISCUSSION

Trade and investment between China and Latin America has increased at unprecedented rates in recent years. This brings with it new challenges and opportunities for collective sustainability efforts. This discussion paper summarises initial evidence on the growing trade and investment between China and Latin America in mining, forestry and agriculture, with a particular focus on Chile, Peru and Brazil. It explores the use and impact of sustainability standards, both international and national – for example, Forest Stewardship Council certification and China's national forestry certification scheme. After analysing the drivers and governance factors shaping the design and uptake of standards, it identifies several important questions for future research, in this under-researched but important topic for sustainability.



The International Institute for Environment and Development is one of the world's top policy research organisations working in the field of sustainable development. With its broadbased network of partners, IIED is helping to tackle the biggest issues of our times – from climate change and cities to the pressures on natural resources and the forces shaping global markets.

### **International Institute for Environment and Development**

80–86 Gray's Inn Road

London, England

WC1X 8NH

Tel: +44 (0)20 3463 7399

Fax: +44 (0)20 3514 9055

email: [info@iied.org](mailto:info@iied.org)

[www.iied.org](http://www.iied.org)