



NewForests

Annual Sustainability Report
FY2011-12

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Message from the Managing Director

New Forests' business grew substantially in 2011-12, and we are now a significant land manager in Australia and poised to continue to grow our business in Australia, New Zealand, Southeast Asia, and the United States in the coming year. As we grow and make new investments, 'the rubber hits the road,' and our commitments to sustainability need to go from theory to practice.

We face continuing questions about what are the right assets to invest in, how those assets should be managed, and how we should do business, often in dynamic or uncertain market environments. At the heart of this process is discipline in decision-making, from our investment committee process to our management committee and our risk and compliance committee. These three committees, along with our Board, are the platform that drives our returns to investors and which supports the implementation of our commitments to sustainable and responsible investing.

We now manage almost 400,000 hectares of land and forestry assets across six Australian states. In many communities we are the largest landowner. Our forestry operations already support hundreds of jobs and will grow over time as we transition to ownership of forestry plantations on the land we manage and we continue to acquire new assets. We want to be successful in generating sound, stable returns, and we recognize that to meet our goals we need to be good members of the business community, exemplary in our forest management systems, and helping to build a sustainable and diverse forestry sector in Australia.

We closed the Tropical Asia Forest Fund in June 2012. This is an exciting development for New Forests and positions us as a true 'impact investor' in a region that has a history of resource extraction and rainforest conversion, rather than sustainable management. In our first fund in the region we seek opportunities that align us with leading firms that share our values and that provide opportunities for steady growth and future investment. With Asia expected to become the centre of global timber demand, there is an imperative to bring long-term institutional investment to the job of establishing a sustainable wood supply.

In the United States we launched Forest Carbon Partners, an innovative investment vehicle focused on the California carbon market. This investment program will help rural landowners to secure conservation finance for their forests. We also continue to manage wetlands and stream mitigation banks, and we have launched a new fund to build a significant position in the growing mitigation banking industry in the United States. The wetlands and conservation banking model in the United States has become the most significant ecosystem-based commercial business model in the world. The concept of no net loss of ecosystems is the ultimate end game for sustainable land management, and we are delighted to be participants in this growing industry.

This is our second sustainability report, and I would like to thank MaryKate Hanlon, our Manager of Sustainability, Research, and Communications, for her work in overseeing our Social and Environmental Management System and in producing this report. Of course everyone in New Forests is part of our sustainability program, and we aim to maintain a set of shared company values. We strive for continuous improvement, transparency, and curiosity in our work and welcome any feedback or questions on how we do business. The question of what is sustainable and responsible investment is ultimately a human construct and may change over time, across regions, and investment strategies. Our commitment is to thinking clearly about the issues, setting a framework that can be monitored, and then reporting on our progress.



David Brand
Founder and Managing Director, New Forests Pty Ltd

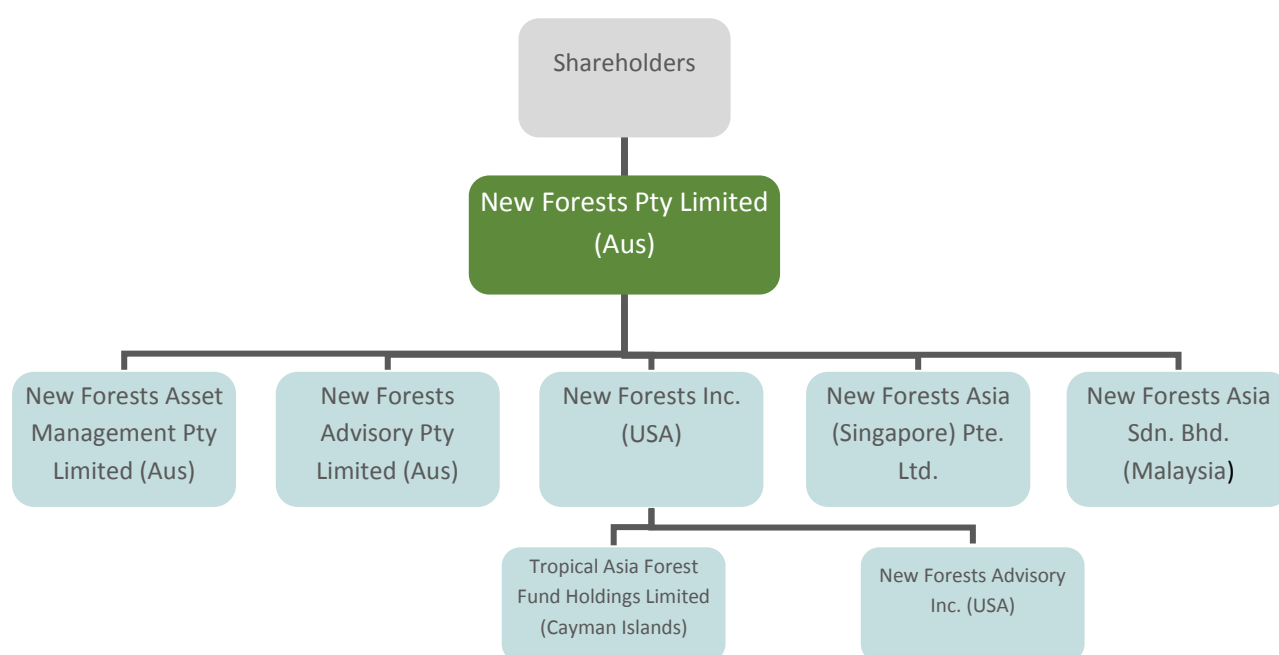
New Forests

Commitment to responsible investment (RI) is central to New Forests' business strategy and corporate culture. Our investment strategies are designed to support a transformative shift of capital into 'natural infrastructure assets' that we believe are a foundation for sustainability. Across all of these activities, the principles guiding our RI approach include environmental, social, and governance (ESG) integration, third-party certification, transparency, and continual improvement. This framework is embedded within New Forests' overall governance and management systems.

New Forests was founded in 2005 and pursued a 'timber-plus' investment model that centred on the sustainable management of forests and ecosystem services. As our company has grown, we have transitioned into a funds management business with a core focus on RI in our asset class. In 2010, we joined the Principles for Responsible Investment and undertook several steps toward the formalization of our sustainability and RI programs; this work is ongoing through the continued development of corporate sustainability and RI initiatives. In this second Annual Sustainability Report, we present our progress and performance in these efforts. This report includes an overview of New Forests, our strategic vision for RI in our asset class, and a discussion of the key elements of our RI framework. It then discusses New Forests' sustainability and RI performance and sustainability targets. Finally, it ends with a discussion of sustainable forest and land management issues in the context of our business, addressing key ESG factors, such as biodiversity, water, and social capital.

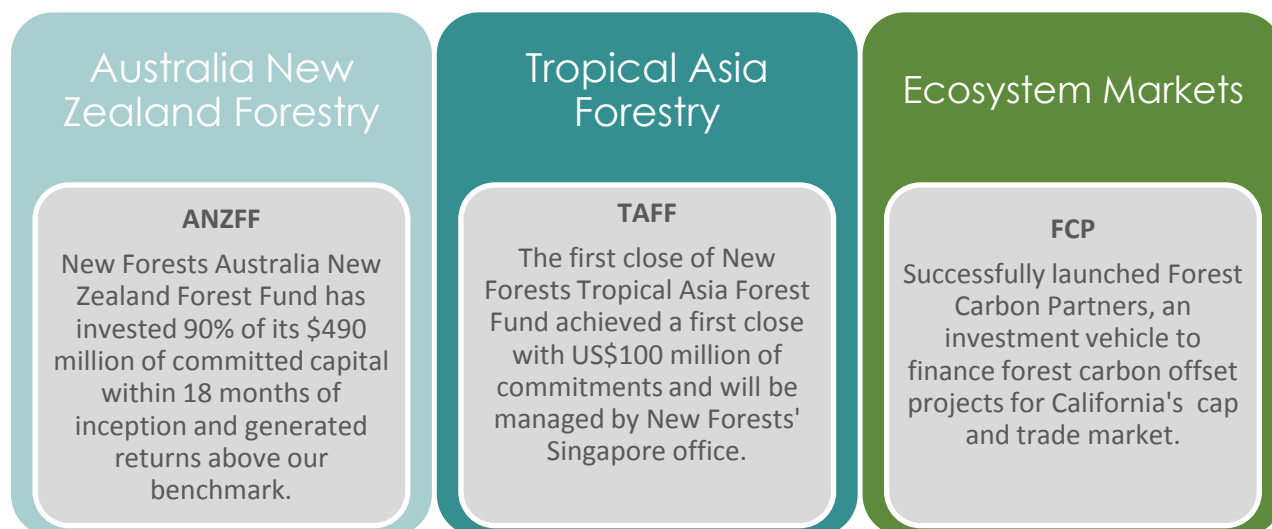
Our Business

New Forests is headquartered in Sydney with offices in Singapore and San Francisco. The company manages over \$1.25¹ billion in commingled funds and separate accounts in timberland and associated environmental markets for institutional and other wholesale investors. New Forests Pty Limited was founded by David Brand and is a privately held company, registered with the Australian Securities and Investments Commission. The company holds an Australian Financial Services Licence. The New Forests group comprises eight companies, including five wholly-owned subsidiaries of New Forests Pty Limited and an additional holding company and subsidiary held by New Forests Inc. in the United States.



¹ Note that all references are to Australian Dollars unless otherwise stated.

Assets under management surpassed \$1.25 billion in FY2011-12, with key milestones achieved across each of our investment strategies.



Investment Programs

New Forests manages over \$1.25 billion in commingled funds and separate accounts in timberland and associated environmental markets for institutional and other wholesale investors. We provide our clients with diversity and choice around risk-adjusted returns, geography, and market exposure through our three investment strategies.

Sustainable timberland investment in Australia and New Zealand

With relatively low risk, stable assets, and well-established markets and management systems, New Forests creates value in the region by buying well, operating effectively in regional timber markets (we have strong relationships in both domestic and export markets for timber from Australia and New Zealand), and providing exposure to emerging markets for a range of bio-energy and bio-materials. New Forests has also been a key player in the rationalization of the forestry Managed Investment Scheme sector in Australia.

Sustainable timberland investment in the growing economies of Southeast Asia

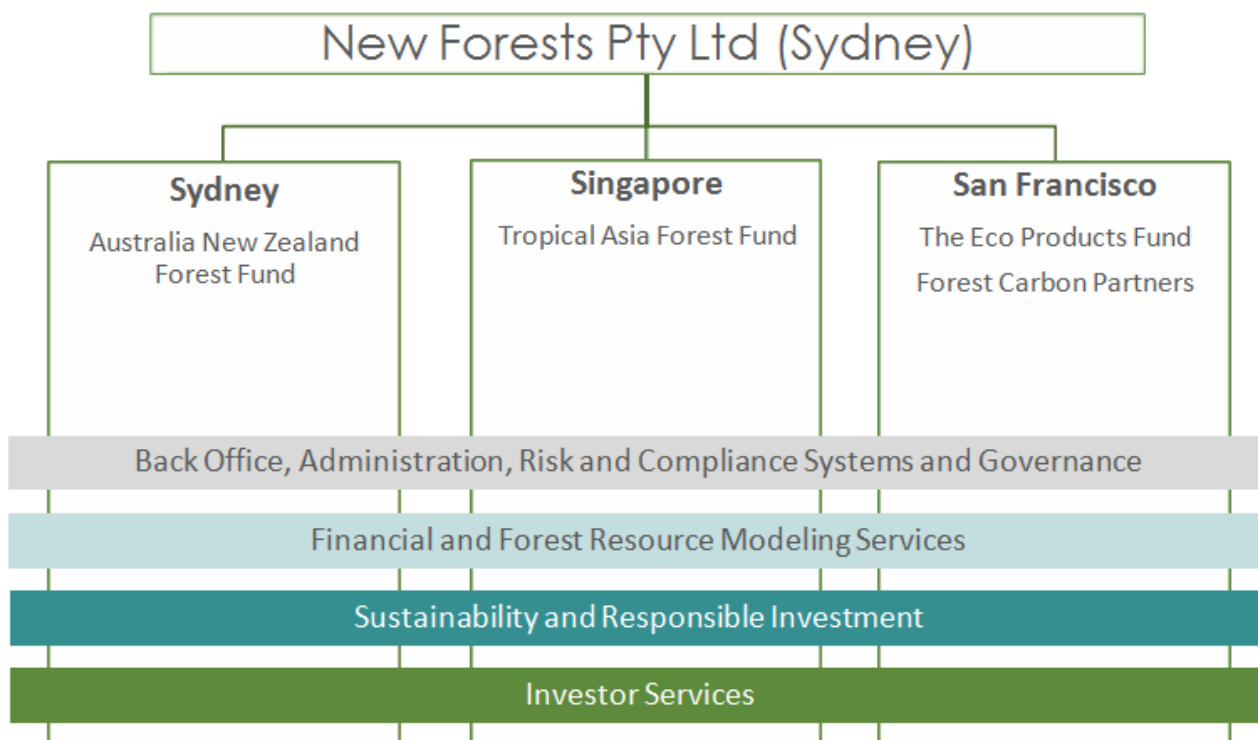
New Forests applies international timberland investment discipline to these high-growth emerging markets and has a particular focus on investment in Malaysia, Vietnam, and Indonesia. New Forests focuses on tropical hardwood timbers (e.g. rubberwood for latex and timber, *Acacia mangium*, sengon, teak) for a variety of end-uses including furniture, flooring, and pulp and paper.

Investment in conservation forestry and environmental markets in the United States

New Forests is expanding its United States business to offer clients strategies in United States conservation forestry and environmental markets with a focus on mitigation banking for wetlands, streams, and endangered species and in forest carbon offset development for California's regulated carbon market. These investments will offer exposure to returns derived from both timber and non-timber values (or ecosystem services) from sustainably managed forest and land systems in the United States.

Functional Structure

To resource our trio of investment strategies, New Forests has developed its business around a management structure that includes centralized corporate funds management services based from our headquarters in Sydney. The investment programs and activities of each fund within those programs are undertaken by regional investment teams in each of our office locations.



Governance

New Forests is committed to conducting business in a responsible and ethical manner. We have in place a governance and compliance framework driven by regulatory compliance (including for the company's Australian Financial Services License); funds management governance, administration, and operational control systems; and our Social and Environmental Management System.



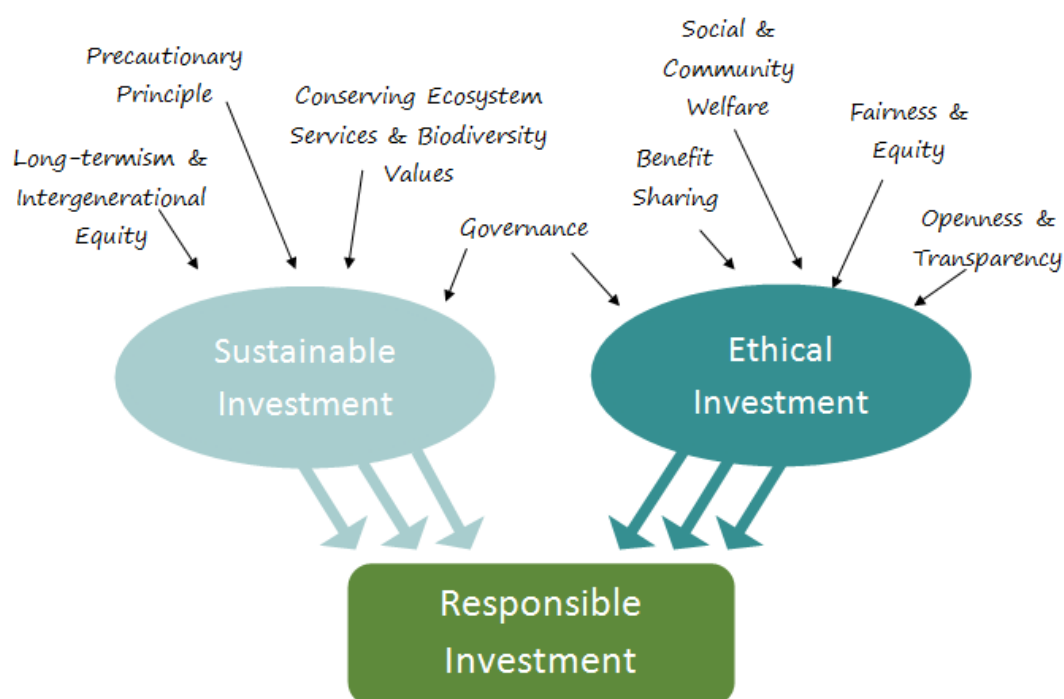
Governance Body	Key Responsibilities
Board of Directors	Approve business strategy and responsible for corporate governance and financial management
Executive Committee	Develop and oversee implementation of company strategy
Management Committee	Determine and manage the strategy for each investment, monitor day-to-day operations, and make key decisions related to our assets under management.
Investment Committees	Review and approve investments and asset sales for New Forests' funds per Investment Committee charter
Risk and Compliance Committee	<p>The objectives of the Risk and Compliance Committee are to assist the board to discharge its corporate governance responsibilities to exercise, due care, diligence and skill on:</p> <ul style="list-style-type: none"> • Internal Control Systems • Risk Management • Complying with applicable laws and regulations • Product development approval

New Forests' View of RI in Forestry & Environmental Markets

For most institutional investors, there is recognition that their investment choices have impacts on the environment and society. Many institutional investors now accept that concepts of ethical and sustainable investment should be implemented to guide the selection and appointment of managers, investment policies for specific asset classes, and reporting practices. New Forests considers ethical investment to be based on trying to define what is 'good' or 'right,' and sustainable investment to be based on the principles of intergenerational equity and fairness. It is important to accept that concepts of ethical and sustainable investment are subjective constructs, which may not be universally held and which may change over time or vary based on circumstances. RI might be considered to encompass both of these concepts as it is centred on ESG risk mitigation. We seek to demonstrate RI in our asset class, forestry and environmental markets, and to practice RI in a way that can be clearly enunciated, monitored, and reported against. New Forests has developed an RI framework that we believe enables our three investment strategies to be delivered in an effective, transparent manner that will meet investor demand for RI products.

Forestry

At a policy level there have been international processes to define sustainable forest management via 'criteria and indicators.' These processes have made significant progress in identifying the key values of forests that are recognized by society—biodiversity conservation, maintaining soils and ecosystem productivity, conserving freshwater catchments, supporting the role of forests in the global carbon cycle, and providing social benefits such as employment, materials for human society, and cultural values. Ethical dimensions include additional considerations around fairness of benefit sharing, respect for both traditional and legal rights, avoidance of corrupt business practices and unhealthy work conditions, and compliance with government regulations and social norms. At an operating level these values have been further refined in the principles of the Forest Stewardship Council (FSC) and the Programme for Endorsement of Forest Certification (PEFC), which provide a basis for third-party certification of sustainable forest management.



For many institutional investors, requiring forest certification has been the primary approach to setting a sustainable and responsible investment policy for the forestry asset class. However, despite the growing use of certification, investors still sometimes encounter negative impacts from ESG risks that fall outside the boundaries of certification, and we believe that this is because of a lack of clear understanding of key issues facing the forestry sector. To practice RI in forestry, managers must have a frame of reference for their investment decision-making and not simply engage in certification as a ‘tick the box’ exercise.

Environmental Markets

As global policy fora continue to grapple with the question of whether and how nature – or rather its ecosystem services – should be priced, investors must consider the risks and opportunities posed by environmental markets. While forestry investors seek to generate returns from the sale of timber, there is likely to be a growing expectation that investments will also shoulder some of the burden of maintaining natural areas, streamside corridors of natural vegetation, and unique habitats found in association with wetlands, rocky outcrops, or unusual soil types. Some investors may undertake this conservation work on a voluntary basis, but experience suggests that it is unlikely to be successful unless there is at least some commercial value placed on the ecosystems and the services that they provide. We are seeing a growing trend toward such price mechanisms and trading schemes. For example, there are existing opportunities that allow forest owners to monetize carbon storage and watershed protection functions provided by forests, to trade in compensatory mitigation of wetlands and endangered species, and to sell easements that restrict the future ability to convert forests to other land uses. These environmental markets have proven to be very challenging public policies to implement. Not only are there active efforts to undermine the implementation of these policies by beneficiaries of the status quo, but there are often criticisms from the environmental movement about pricing nature or allowing nature to become a commodity.

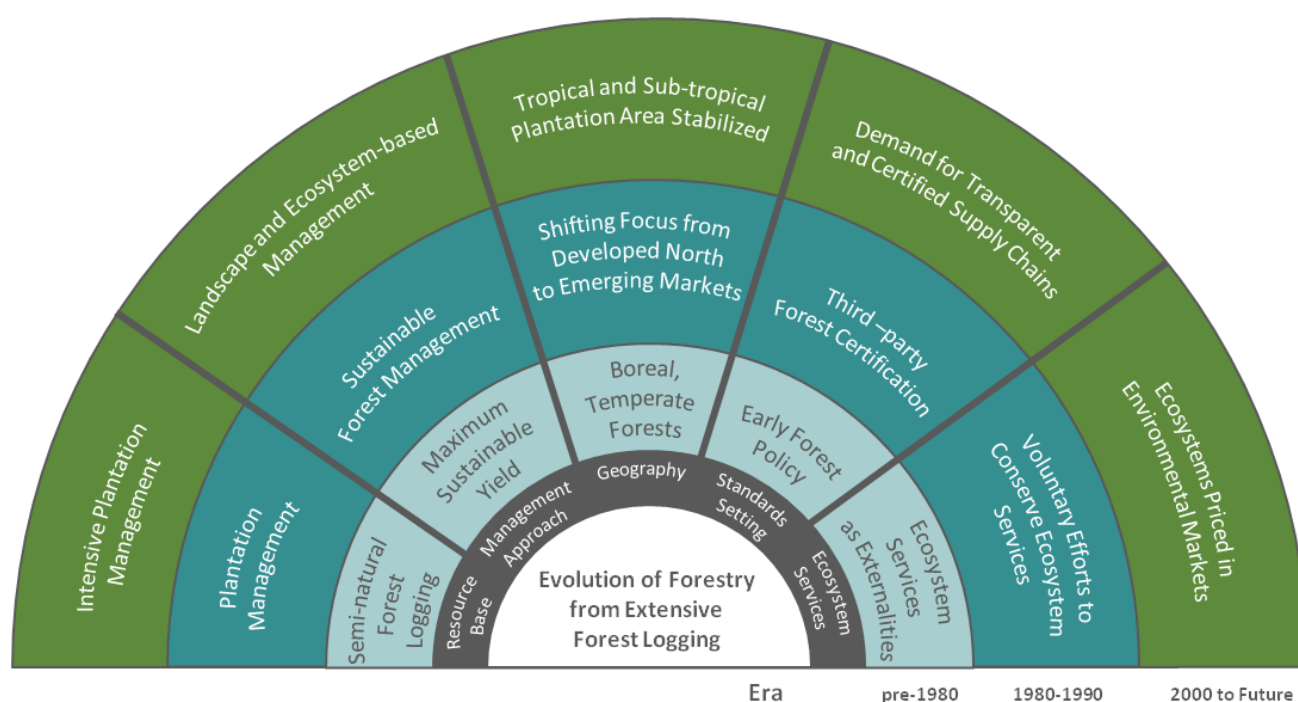
Investing directly into assets whose core revenue streams are derived from environmental markets is generally outside the scope of institutional investment as these markets are still either too small or present uncertain risk return characteristics. However, accessing opportunities to commercialize ecosystem services in association with forestry assets offers the potential to generate multiple revenue streams and can help mitigate the costs of conservation measures.

Sustainable Asset Classes

New Forests believes its investment strategies encapsulate sustainable asset management and that by promoting RI in forestry and environmental markets we are differentiated as a manager. By bringing institutional capital to support investment in these sectors, New Forests contributes to the stabilization of long-term investment in renewable resources (principally wood products) and ensures the conservation and protection of ecosystem services associated with our investments. Ultimately, we believe capital must flow toward land management systems that value both production and conservation functions.

New Forests has developed an approach to RI in forestry and environmental markets that we believe addresses key sustainability risks and opportunities. In particular, we have articulated this approach to forestry investment in our publication *Responsible Investment in the Forest Sector: Recommendations for Institutional Investors*.² Our ability to develop and execute forward-thinking investment strategies is supported by this view of the long-term sustainability of the assets and sectors in which we invest. Alongside the evolution of forestry plantations into an institutional asset class, there is also growing consensus on the need for holistic solutions that integrate production and conservation efforts at a landscape scale and mechanisms like third-party certification that provide transparency through supply chains to consumers on the underlying source of wood products. A key part of the evolution to a stabilization of natural forests will be successful implementation of new markets for ecosystem services like carbon, biodiversity, and water catchment protection. While these eco-markets are still in their early stages, we expect that they will be supported by investors and will in turn reward investors who take a wider view of their responsibilities and the social and environmental outcomes from their investments.

Institutional investment can bring capital to transform forestry and support environmental markets – thus addressing global ESG issues and creating long-term value.



² Available at: [http://newforests.com.au/news/pdf/articles/Responsible Investment in Forestry.pdf](http://newforests.com.au/news/pdf/articles/Responsible%20Investment%20in%20Forestry.pdf)

New Forests' Responsible Investment Framework

New Forests has created an RI framework that supports our three investment strategies in delivering an effective, transparent response to our clients' demand for RI products. As part of ongoing efforts to formalize our RI practices, New Forests has integrated its RI framework within the company's governance and management structures. Sustainability programs are monitored by a dedicated ESG staff person based in Sydney. The implementation of sustainability and RI practices, however, occurs at all levels of the investment process and involves nearly all members of New Forests' staff.

Our corporate approach to sustainability and RI is built around three complementary commitments:

Principles for Responsible Investment (PRI)

Managed at the corporate level, New Forests is a signatory to the PRI, which requires the company to integrate six ESG principles into investment activities and decision-making.

New Forests Social and Environmental Management System (SEMS)

The New Forests SEMS coordinates corporate-level, fund-level, and asset-level activities related to social and environmental management and is based upon internationally recognized standards of performance.

Sustainability Reporting

New Forests conducts several levels of sustainability and RI reporting. Our quarterly fund reports provide updates on key sustainability issues for fund assets and related markets, progress toward forest certification (where relevant), and other pertinent ESG information. In addition, we annually report to the PRI and issue our Annual Sustainability Report. The Annual Sustainability Report is a means of taking stock of our company-wide efforts to be a leading responsible and sustainable investment manager and of reporting publicly on our progress.



Principles for Responsible Investment

The Principles for Responsible Investment (PRI) initiative is a network of more than 1100 institutional investors, investment managers, and service providers working together to put the Principles (see below) into practice. PRI is an investor-led initiative in partnership with the UNEP Finance Initiative and the UN Global Compact. The Principles reflect a shared perspective that ESG issues can affect investment performance and should be given appropriate consideration by investors.

As part of New Forests' commitment to the PRI, the company participates in the annual PRI Reporting and Assessment survey. New Forests joined the PRI as a signatory in 2010, and 2011 was the company's first year participating in the assessment and review process.

The Principles for Responsible Investment

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

- P1. We will incorporate ESG issues into investment analysis and decision-making processes.
- P2. We will be active owners and incorporate ESG issues into our ownership policies and practices.
- P3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.
- P4. We will promote acceptance and implementation of the Principles within the investment industry.
- P5. We will work together to enhance our effectiveness in implementing the Principles.
- P6. We will each report on our activities and progress towards implementing the Principles.

www.unpri.org

2011 PRI Performance

In 2011, New Forests reported on the calendar year 2010 for PRI performance. Recognizing that 2010 was New Forests' first year as a PRI signatory and that new sustainability procedures were put into place mid-calendar year, the company performed well on its initial assessment. New Forests' best performance was relative to our investment management peers that also signed on to PRI in 2010, which may indicate that the company's sustainability orientation and early work on the SEMS were beneficial. Our best performance for any of the Principles was for P2, which reflects strong incorporation of ESG issues into ownership policies and practices. The figure below notes these highest ranking scores as well as the areas in which New Forests exhibited the lowest scores.

New Forests aims to perform in the first or second quartile for all categories in the PRI annual assessment and reporting.

Highest Scores

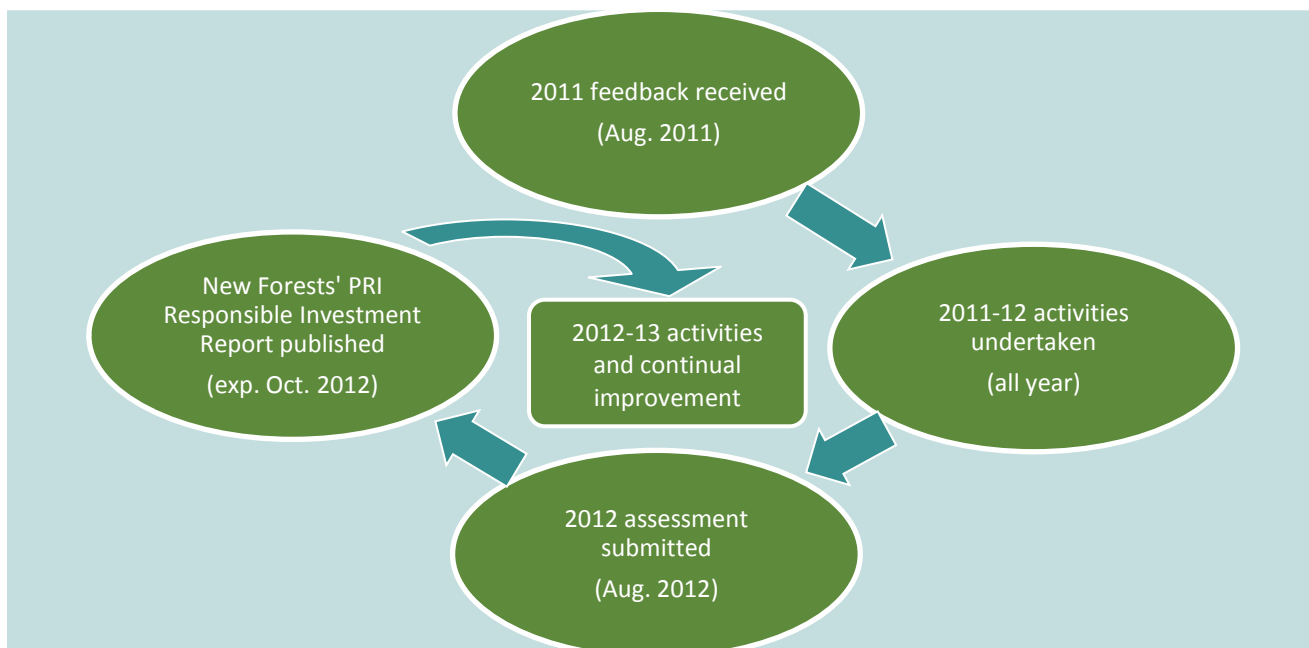
- Top quartile ranking for P2 against peer Investment Managers signed in 2010.
- Top quartile ranking for P2 against all peers, except for IMs with mainly non-listed real estate (2nd quartile).

Lowest Scores

- For P3, P5, and P6 New Forests ranked primarily in the third quartile against the peer groups. In part, this is a reflection of the fact that we were not PRI participants for the full year and did not have the benefit of a full year for engagement.
- For P6, New Forests ranked in the fourth quartile against all Investment Managers in Australia. This is the company's only bottom quartile ranking, and given that this principle relates to reporting, it should improve steadily over time as we undertake our reporting consistently over time.

2012 PRI Outlook

New Forests utilized our 2011 feedback report as a basis for advancing our implementation of the Principles over the past year, and we believe these actions will support improved performance in the 2012 reporting and assessment. In 2012, PRI piloted a new online reporting tool, and we opted in to the voluntary reporting process to support the pilot and provide continuity in our reporting. One challenge was that there was no sector-specific supplement relevant to our asset classes, so we were not able to input more detailed answers that demonstrate the depth of our ESG approach in forestry. Our communications with PRI indicate that they hope to have a forestry-specific sector supplement available in future reporting years. Our inputs were submitted in August 2012 for the financial year 2011-12, and we will receive a copy of our Responsible Investment report from the PRI around October. We intend to share this report publicly, including on our website and by offering it to our existing and prospective clients. This is an important component of our efforts to increase transparency in our RI activities and to promote PRI. Again this year, we will again engage in an internal review process regarding our PRI performance and areas for improvement.



Collaborating for Biodiversity Links – Green Triangle, Australia

In Australia's Green Triangle region, New Forests collaborates with the local Catchment Management Authorities (CMA), who are charged with integrating community involvement with natural resource decision making and management. The Glenelg-Hopkins CMA sought to create biodiverse carbon sinks through reconnecting key habitat, improving the resilience of existing habitat, and controlling pest plants and animals in a series of "biolinks" within a regional biodiversity hotspot. New Forests participated in the CMA's application to the Government's Biodiversity Fund, identifying synergies in the CMA's biolinks programs across New Forests' hardwood and softwood properties in the region. Priority properties have been selected based on location and potential environmental values on site as well as the properties' role within the regional natural resource planning.

Currently, New Forests is working with the CMA to further develop implementation plans for the biolink development, and we expect that riparian and wetland areas will be planted with a mixture of local plants to produce a biodiverse carbon sink and restore native vegetation. Anticipated outcomes for our hardwood plantation properties include improved species diversity, protecting priority plant species, and enhancing environmental function. From an investment perspective, our collaboration with the CMA is not only an important part of our stakeholder engagement for supporting forest management certification but is also a means to achieve physical outcomes that improve environmental qualities on our forestry properties.



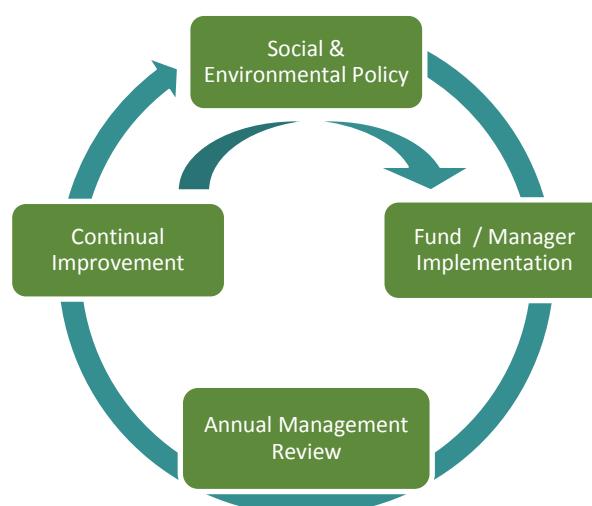
Social and Environmental Management System

The central element of our RI framework is our Social and Environmental Management System (SEMS). New Forests' SEMS is framed around approaches established in the ISO 14001 series. The SEMS is designed to systematically identify, manage, and report on social and environmental aspects and potential impacts of New Forests' investments by:

- Establishing a consistent approach to social and environmental management across all investment activities;
- Monitoring performance and identifying areas for corrective action;
- Providing management controls to ensure corrective actions are taken and lead to continual improvement in performance; and
- Ensuring management review and Board-level oversight of the system as a whole.

This approach delivers consistency in RI approach and implementation, appropriate to our firm's size and reach.

A key aspect of SEMS governance is an internal annual audit conducted on each fund vehicle. The SEMS manager conducts the audit based on materials provided by portfolio managers, investment analysts, and asset management staff as well as through interviews with related staff. The audit assesses compliance with the social and environmental policies and implementation responsibilities under New Forests' SEMS. The audits are reviewed by the company's corporate Risk and Compliance Committee.



Certification and Standards Guidance

New Forests' SEMS policy documents include a Social and Environmental Policy that is framed around the use of internationally-recognized third-party standards and certification schemes. As New Forests primarily invests in forestry, rural land (generally timberland), and environmental markets asset classes, our policies are designed to address the social and environmental risk factors appropriate to these assets and the geographies in which we invest and operate. For forestry assets, we seek to achieve forest management certification with the Forest Stewardship Council (FSC) for all eligible assets. In cases where an asset is not eligible for full FSC certification, an alternate standard will be selected. For forestry plantations in tropical Asia, if full FSC certification is not available, for example because of past conversion of natural forest areas, we will still undergo independent certification for compliance with all other FSC criteria. In addition, our Tropical Asia Forest Fund also requires us to achieve compliance with the International Finance Corporation's Performance Standards (IFC Performance Standards). For wood processing assets anywhere, we must comply with the IFC Performance Standards. Each of our investment funds has a certification policy that provides additional guidance and specificity around processes for achieving and maintaining appropriate certifications.

Clear performance measures and independent verification provide guidance for fund managers and transparency to stakeholders.

	Australia New Zealand Forestry	Tropical Asia Forestry	Ecosystem Markets
Forestry	FSC or FSC Alternate (e.g. Australian Forestry Standard)	FSC or FSC Alternate, with verification against all eligible FSC criteria	N/A
Environmental Markets	<p>Where possible, achieve legal requirements for social and environmental performance as defined in protocols, rules, or methodologies under a compliance regime (e.g. Carbon Farming Initiative, New Zealand ETS, or biobanking)</p> <p>For other voluntary environmental markets (i.e. biodiversity, water), identify appropriate recognized standard</p>	<p>For carbon achieve Verified Carbon Standard (VCS) plus Climate, Community & Biodiversity Standard Alliance (CCBA) certification for voluntary carbon projects (unless compliance schemes develop)</p> <p>For other voluntary environmental markets (i.e. biodiversity, water), identify appropriate recognized standard</p>	<p>Where possible, achieve legal requirements for social and environmental performance as defined in protocols, rules, or methodologies under a compliance regime</p> <p>Achieve Verified Carbon Standard (VCS) plus Climate, Community & Biodiversity Standard Alliance (CCBA) certification for voluntary carbon projects in developing countries</p> <p>For other voluntary environmental markets (i.e. biodiversity, water), identify appropriate recognized standard</p>
Land	Manage all land assets in compliance with government laws, regulations, and best management practice guidelines for the jurisdiction and land uses concerned		
Infrastructure	Ownership of any kind of wood processing facility requires verification audits that management plans adhere to the IFC Performance Standards.		


2011-12 SEMS Performance

Over FY2011-12, two funds – New Forests Australia New Zealand Forest Fund and Forest Carbon Partners – went through a complete annual auditing cycle of the SEMS. Annual audits for ANZFF and Forest Carbon Partners were conducted in May and June and finalized and reviewed by the Risk and Compliance Committee in July 2012. While the reviews identified some weaknesses and areas for improvement, no corrective actions were identified and both funds are in compliance with relevant policies.

2012-13 SEMS Outlook

Over the coming year, New Forests will conduct a review and update of the SEMS as part of the continual improvement cycle. In particular, the SEMS will be updated for the following aspects:

- Incorporating lessons learned from first two years of implementation;
- Updating asset class guidance to potentially include management standard guidance in addition to certification scheme guidance; and
- Allowing for demonstration and monitoring of other sustainability and stewardship activities not captured by current process.



Transformative Investment in Southeast Asian Tropical Forestry

In June 2012, New Forests announced the first close of the New Forests Tropical Asia Forest Fund (TAFF) with commitments of US\$100 million. TAFF is the first private, closed-end investment fund with a dedicated focus on plantation forestry assets in the tropical Asia Pacific region. The Fund is also the first commingled fund offered in New Forests' Tropical Asia Forestry investment strategy.

TAFF's investment mandate primarily focuses on new and existing Forest Stewardship Council (FSC) certified timber plantations but can also include limited natural forest concessions and timber processing facilities in Southeast Asia. The Fund will implement a certification policy and will be supported by New Forests' Social and Environmental Management System. This includes complying with IFC Performance Standards and attaining FSC certification for its assets. TAFF may also invest in environmental assets that can profit from a growing demand for forestry related carbon offsets (including REDD) and biodiversity offsets. To support this opportunity, the Dutch Development Bank, FMO, has made a €200,000 grant to TAFF for carbon and biodiversity project development.

Tropical Asia represents a frontier market for forestry investment, and TAFF is a first of its kind investment program. The Fund will invest entirely in emerging market economies, with a focus on Indonesia, Malaysia, and Vietnam. TAFF offers institutional investors exposure to a region with strong growth in demand for tropical hardwood timber and a long history and technical expertise in forestry and agribusiness plantations.

By bringing New Forests' core focus on sustainable and responsible investment in forestry to our work in tropical Asia, the company seeks to improve performance from management of social and environmental issues as part of our focus on generating excellent investment returns. The TAFF investors recognize the triple bottom line returns available through their investment in TAFF.

Sustainability Targets

New Forests' targets for sustainability are incorporated in business plans, investment mandates, and in our first Sustainability Report. Initially, these targets have been focused around the development and implementation of our core sustainability systems and functions. As our sustainability and RI programs continue to mature, these targets will increasingly encompass more sophisticated and ambitious sustainability goals in line with our overall business planning.

2011-12 Target Activities	Status
Build on 2010-11 initiatives of joining PRI and producing our first sustainability report to continue to differentiate ourselves as a sustainable and responsible investment manager	In September 2011, New Forests received its first PRI feedback report, which was utilized as a basis for designing a program of works to strengthen sustainability and ESG integration across the company.
Complete first full year of implementation of the SEMS	During the year, two funds (ANZFF and FCP) were subject to the SEMS, and the complete annual management cycle took place. Internal audits were conducted from May to June and found no corrective actions necessary.
Relocate the corporate sustainability functions to headquarters and transition sustainability responsibilities from outgoing director	In September 2011, the role was relocated to Sydney office, enabling greater integration of sustainability programs and ESG incorporation across company's activities.

Over the coming year, New Forests seeks to continue its progress in demonstrating RI in our asset classes and distinguishing ourselves as a sustainable and responsible investment manager. In line with these objectives, we have determined the following priorities for FY2012-13.

Enhance staff alignment with sustainability and RI objectives

Currently, a number of New Forests' staff have responsibilities relating to sustainability and RI implementation, with monitoring and oversight responsibilities at the portfolio manager, SEMS manager, executive committee, and Board levels. Yet in some cases these activities are not explicitly linked to position descriptions, KPIs, and performance evaluations. Possible actions include:

- Incorporate sustainability and RI activities in position descriptions
- Develop KPIs related to sustainability and RI for all positions where relevant
- Investigate opportunities to align long-term sustainability performance with staff incentives

Increase transparency & visibility of our Sustainable and Responsible Investment activities

RI includes leading by example, and it is important that New Forests promote RI within timberland and environmental markets investment. Increasing the visibility of our RI approach will support our business goal of differentiating ourselves as a leader in sustainability and RI.

- Publish and share our Responsible Investment Report as generated by the PRI 2012 Reporting and Assessment tool
- Create a sustainability and RI section on our website to promote transparency of our policies and information sharing
- Build on our sustainability reporting capacity, including corporate reports and client reporting

Develop framework of measurable sustainability indicators

Indicators can provide a consistent method of assessing performance over time, and a growing body of sustainability indicators is emerging. New Forests is also seeing increasing interest from clients in the use of standardized qualitative and quantitative ESG metrics. It is important that we understand which indicators or metrics are most suited to our business and sustainability impacts.

- Investigate potential for use of quantitative sustainability metrics
- Demonstrate how an emphasis on sustainability and RI-related management and performance adds value to our investments.

Perform within the 1st or 2nd quartiles for all PRI assessment criteria

The PRI is the leading international effort for RI involving institutional investors. The framework provides a quantitative means to assess our performance in RI, and the New Forests business plan has identified improving PRI performance as a business target. In 2012, the PRI piloted a new reporting framework and no individual feedback reports will be provided this year. As such, we will be working toward meeting this goal over the coming year, using our 2013 reporting and assessment to review our progress.

- Utilize 2012 PRI Responsible Investment report and other PRI feedback as a means to develop actionable work plan for improvement
- Incorporate senior management and Board in RI performance strategy

Pioneering Carbon Investments to Help Conserve US Private Forests

Forest Carbon Partners, L.P. is an investment vehicle managed by New Forests, which finances forest carbon offset projects for the California cap and trade market. Forest Carbon Partners identifies and originates projects with non-industrial forest owners, primarily family forest owners and Native American tribes; finances and manages project development; and markets issued offset credits to compliance buyers and financial intermediaries in the California cap and trade market.

New Forests has been an early and active investor in the California offset market through previous investment programs, and Forest Carbon Partners alone has financed improved forest management projects on over 15,000 acres to date. These projects will encourage the maintenance of older-growth forests, protect wildlife habitat, and deliver significant revenue to rural landowners and tribes. We expect to develop offset projects that accomplish forest conservation on well over 100,000 acres of forests through Forest Carbon Partners by 2014.

New Forests has developed its United States forest carbon investment strategy over more than four years of active engagement with market participants, regulators, and other stakeholders. We implemented a proactive strategy to promote investment-friendly regulations that we believe will help deliver investment to produce multiple benefit carbon projects. In particular, New Forests engaged with regulators and standards bodies to support development of 'aggregation' protocols that enable owners of smaller forest-holdings to have access to carbon markets through achieving economies of scale in aggregated projects. Development of intellectual property around environmental markets is an important area for New Forests' business growth, and our success in launching Forest Carbon Partners demonstrates the rewards of cultivating intellectual capital.



Sustainable Management of Forests and Environmental Assets

Responsible and environmentally sustainable management of land and natural resources is central to New Forests' investment philosophy and corporate culture. We are committed to this kind of management approach not only for risk management purposes but also because of commercial opportunities associated with innovative approaches to sustainable forestry and land management. Both global and local issues can present challenges that require careful consideration of ESG factors. On the other hand, sustainable management of forests and environmental assets offers the potential to increase total returns by generating new sources of revenue.

Global and Macro Issues

New Forests' business is at the forefront of addressing some of the world's most pressing social and environmental issues, including climate change, loss of biodiversity and other ecosystem services, and growing global demand for commodities and primary materials. We seek not only to mitigate these risks through our investment strategies, but also to view them as opportunities to promote a shift toward sustainable investment that balances economic, environmental, and social pressures on the land, and in particular forests. Because the mitigation of these risks requires innovation and significant expertise, New Forests views our experience in developing and executing investment strategies that focus on these key themes to be a competitive advantage.

At the same time, these and other social and environmental factors also produce local risks that may affect our business. Some issues of concern include:

- Climate change may increase the likelihood of damaging and catastrophic weather events, including cyclones, drought, wildfire, and insect or disease infestations
- Growing demand for palm oil, soy, beef, and other agri-commodities creates increasing pressure for land, which can impact timberland highest and best use (HBU) value and rural land markets
- Concerns about land grabbing and agricultural production create a highly sensitive environment for international investors and may add regulatory and political uncertainty to investment programs.

Local Issues

Putting sustainable management into practice on the land is not always easy or clear. While our SEMS has defined objectives for meeting internationally recognized standards of practice, challenges do arise in asset management. These challenges require an adaptive management capacity that can evaluate management alternatives and find successful pathways that do not compromise management standards or financial performance. Some examples of asset management questions that have arisen over the past year include:

- What is our obligation as the seller of land to ensure sustainable future management of the property being sold?
- How do we balance certification requirements with conflicting requests from government and local resource management agencies?
- Where forestry plantations have been acquired from failed Managed Investment Schemes and will be returned to agriculture because of sub-commercial prospects, do we undertake FSC certification of these plantations while we are managing them?

New Forests and Integrated Reporting

New Forests engages in many types of reporting as part of our business, some of which are compliance obligations and others driven by our desire to provide high-quality service to our clients. While sustainability and RI are included within these other reports, New Forests is now producing its second Annual Sustainability Report, which directly addresses the integration of sustainability and RI across our business.

Integrated Reporting is a new approach to corporate reporting that seeks to integrate the environmental, social, and economic context within which a company operates with its corporate reporting. It reinforces connections between ESG, performance, and company strategy. The International Integrated Reporting Council leads the development of a global framework for Integrated Reporting, with support from leading international companies and networks, such as the PRI. Integrated Reporting can help businesses and their stakeholders assess a company's sustainability from environmental, economic, and social perspectives and includes an emphasis on connectivity between sustainability and business performance, with particular attention to six categories of capital: **financial, manufactured, human, intellectual, natural, and social**. Although this report is not a fully Integrated Report (due to the evolving nature of our reporting and because as a private company we do not publicly report on financial performance), we do address the aspects of Integrated Reporting throughout this report and directly in brief below.

Financial Capital

New Forests' business is based on the unique characteristics of forests as appreciating assets with no fixed maturity. Trees grow and build value over time and can be harvested over extended periods of time as market conditions dictate. For institutional investors this gives very low volatility relative to the returns and contributes to improving the overall risk efficient frontier in portfolio design. It is this biologically based return, along with the ability for forests to be renewable in perpetuity, and to produce low embodied energy materials, that makes timberland and environment markets leading sustainable asset classes.

Financial capital: AUM grew from \$938 million to more than \$1.25 billion.

Manufactured Capital

New Forests' forestry investment strategies relate to global timber supply chains, and our environmental markets strategies relate to several sectors including infrastructure, energy, and transport. Despite these relationships, as a financial services company we are focused on the management of the underlying natural resource—the forest—rather than the manufacture and production of goods. Nevertheless, as significant managers of forest plantation area, New Forests is involved in the supply of renewable raw materials that are in turn used for a variety of end uses.

Manufactured capital: New Forests' Australian softwood estate supplied 427,000m³ radiata pine timber, a sustainable & renewable material.



Human Capital

Over seven years, New Forests has grown from an initial staff of four to 25 employees today. We now have full-time staff working in three dedicated offices and in four countries. One of New Forests' greatest assets is the diversity, depth, and breadth of experience in this team. Our company has a unique complement of backgrounds, which enriches our work in many ways. As we grow, we seek to maintain a strong company culture, including high levels of information sharing and communications, teamwork, and a celebration of innovation and entrepreneurship. To support this, New Forests' management seeks to operate in an open and transparent manner and to view our employees as key stakeholders in the company. We also seek to foster employee growth and promotion through our training programs, which include annual review and identification of opportunities for formal and informal training. These resources are an important means to ensuring New Forests continues to grow our human capital in more than just numbers.

Human capital: Our team of 25 brings a diversity of backgrounds and qualifications with staff expertise spanning forestry, real estate, business and financial services, environmental management, and law.

Intellectual Capital

Fostering our intellectual capital is paramount to New Forests' growth and future success. We are differentiated by our forward-looking investment strategies, emphasis on market research, and leadership in sustainable land and forestry management. New Forests has an established market research function incorporated as part of our corporate services. In addition, staff from across the company contribute to these research efforts, ensuring the specialist skills and market intelligence of our team is used to advance our research and development of investment strategies. An editorial calendar to formalize and structure these efforts has been designed and implemented for FY2012-13. New Forests is also active in its industry network in ways that share and promote intellectual capital. We are members, sponsors, and contributors to working groups, industry associations, conferences, and publications.

Intellectual capital: In FY2011-12, we published three book chapters:

- "Institutional Investment in Sustainable Forestry" in *Forests for People* (United Nations Forum on Forests for the International Year of Forests)³
- "A Perspective on Timberland Investment" in AP2 10th Anniversary Anthology (Second National Swedish Pension Fund)⁴
- "New Opportunities and Market Restructuring" in *Sustainable Forestry Funds 2012* (Environmental Finance)⁵

Natural Capital

New Forests' business is founded on strategies that should positively impact on the world's natural capital. This takes place through our investment activities in terms of on-the-ground sustainable land management practices as well as by promoting the shift of investment capital into sustainable assets. Natural capital outcomes and impacts are focused primarily on forests, biodiversity, and water.

Natural capital: Three investment strategies that directly incorporate ecosystem services and sustainability into our investment theses.

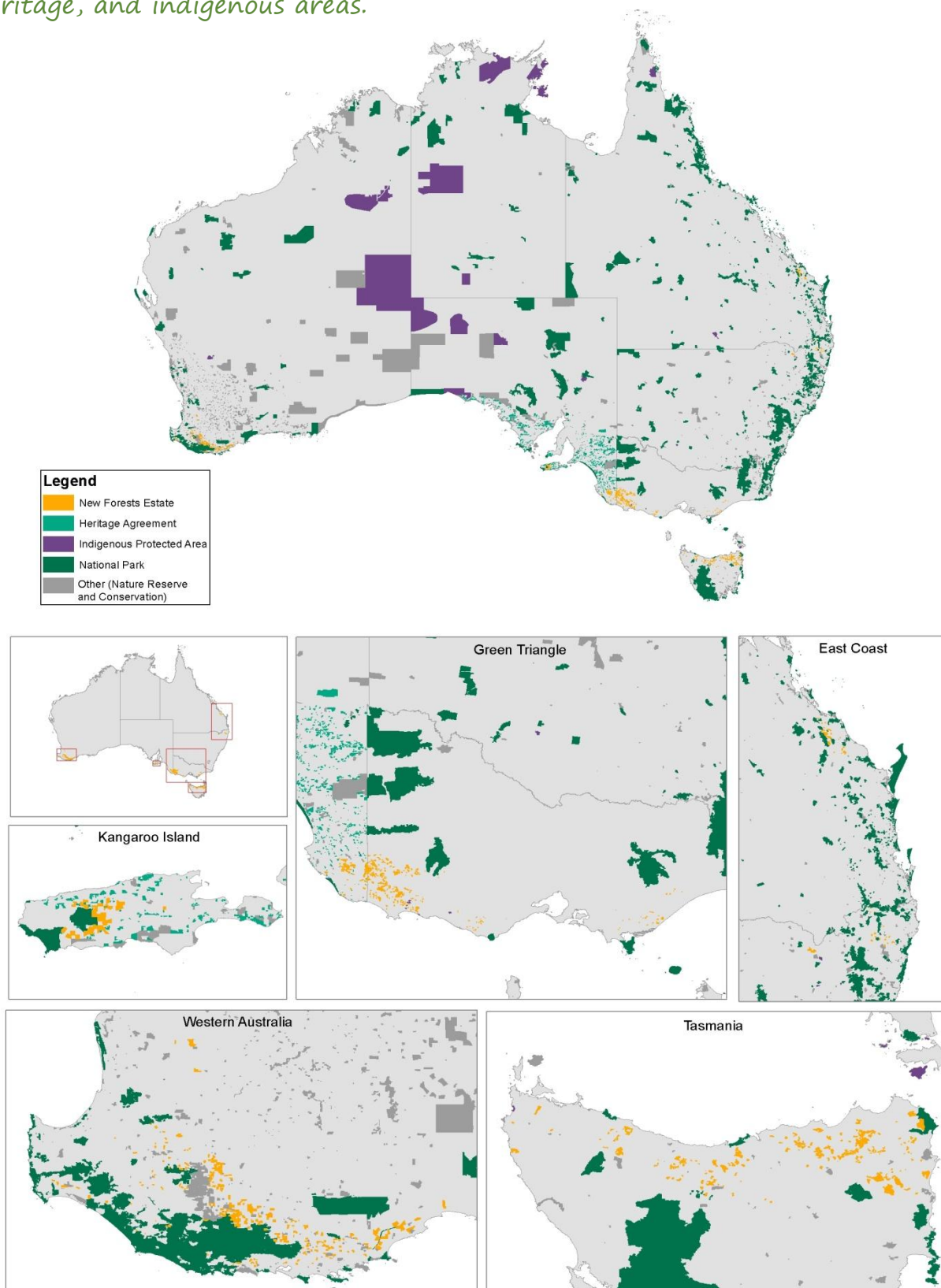
³ Available at: <http://newforests.com.au/news/pdf/articles/UNFFchapter.pdf>

⁴ Available at: http://newforests.com.au/news/pdf/articles/Responsible_Investment_in_Forestry.pdf

⁵ Available at: <http://www.environmental-finance.com/books/view/14>

Our estate in Australia –

New Forests' timberland estate is interwoven with protected, conservation, heritage, and indigenous areas.



Maps based on New Forests' data and Collaborative Australian Protected Areas Database. Only partial data was available for Victoria State.

Forests

Our forestry investment strategies seek to promote the sustainable supply of wood products to meet growing global demand without compromising the status of remaining natural forests. As the only timberland manager focused on the Asia Pacific region, New Forests works across different forest ecosystems and engages in appropriate management strategies that provide financial returns, social benefits, and environmental stewardship.

In Australia and New Zealand, our investments focus solely on plantation timberland. In Australia, this may be either hardwood (i.e. eucalyptus) or softwood (i.e. radiata pine) plantations. Our investments in Australia seek to contribute to the stabilization of the forest sector, which is undergoing a period of restructuring. In particular, the Managed Investment Scheme industry has collapsed, leaving extensive eucalypt plantations in need of a more sustainable business model. We believe our investment strategy will bring a long-term perspective to the management of these areas, including consolidating properties into a sustainable, productive estate and returning other properties to their highest and best use. In New Zealand, radiata pine plantations form the principal investment opportunity. We appoint professional property management companies for local operational management and seek to achieve forest management certification under the Forest Stewardship Council or Australian Forestry Standard.

In tropical Asia, our investment program will focus primarily on sustainable timber plantation assets in Malaysia, Indonesia, and Vietnam. All forests will be certified to the Forest Stewardship Council and also achieve compliance with the International Finance Corporation's Performance Standards. If a forest plantation is not eligible for FSC certification, it will be verified for compliance with all applicable criteria.

Through Forest Carbon Partners, our investment in carbon project development includes the sustainable use of forests for carbon offset production in the United States. We work with non-industrial forest owners to develop carbon projects that ensure long-term environmental benefits via greenhouse gas emissions reductions. Initial project lands in Forest Carbon Partners are predominantly old growth redwood forests, with a mixture of oaks and other native tree species.

Biodiversity

All three of New Forests' investment strategies engage in sectors that have direct biodiversity impacts, and indeed some of our investment models seek to realize the value of biodiversity in association with forestry assets or directly through biodiversity markets. The management of biodiversity is a priority for New Forests as part of our commitment to responsible and sustainable forestry and land management.

In Australia, we are a significant land manager with nearly 400,000 hectares of land across six states. This area includes the country's most iconic species, such as koalas and kangaroos, as well as some of the most endangered, like the Tasmanian devil. Under forest management plans and documentation required for forest certification, biodiversity surveys are undertaken to identify and track species that occur in the plantation and surrounding area. New Forests also engages with local and regional resource planning agencies on opportunities and projects to protect and restore critical areas for biodiversity. Over the last year, New Forests successfully collaborated with a Catchment Management Authority to receive funding for projects creating biodiversity corridors in the Green Triangle, one of our primary forestry operating regions.

New Forests has been a leader in biodiversity markets in Asia since the 2008 launch of the Malua BioBank, an innovative conservation investment and 34,000-hectare project in Sabah, Malaysia on the island of Borneo. The Malua BioBank restores and conserves wildlife habitat for threatened and endangered species,

such a Sumatran rhino and orangutans, and sells Biodiversity Conservation Certificates to companies associated with the palm oil supply chain and to retail customers through www.protectmalua.com. As our Tropical Asia Forest Fund was closed in June 2012, we are now positioned to utilize our experience in this voluntary biodiversity market project within our forestry fund. Many forestry assets throughout Asia include areas of degraded natural forest or unlogged natural forest that could be managed for biodiversity protection as part of conservation set-asides associated with timber plantations. While all projects will include biodiversity surveys by local experts and consider biodiversity maintenance and issues in forest management plans, there is also potential to replicate the biobanking investment model in association with core timber plantation investments.

In the United States, regulatory markets for biodiversity are called conservation or species banking, authorized under the Endangered Species Act. Over the past year, New Forests has designed and launched a new fund that will raise capital to invest in conservation banking as well as mitigation banking, which is focused on wetlands conservation and restoration. Both conservation and mitigation banking are important market systems for ensuring ecosystem restoration and protection, which supports biodiversity.

Water

Water resources are vital to the sustainability of the world's forests and ecosystem services. Our business has material impacts on water in several ways; however, measurement of these impacts is difficult.

Water is a particularly important resource in the Australian context, where water conservation has been a key public policy issue. To support these efforts, New Forests works with Catchment Management Authorities (government agencies charged with integrating natural resource management with local communities) in the areas in which we hold land and/or forestry assets. This helps ensure our properties contribute to shared objectives in conserving and strengthening the functioning and management of Australia's water resources. In addition, plantation forestry has been noted as a management approach for achieving a salinity benefit in targeted areas experiencing adverse effects from dryland salinity, particularly in rural Australia. Some of our assets under management occur in such locations; ongoing management of these properties and potential for land use changes (e.g. tree harvest followed by conversion to agricultural land) may in turn have water-related impacts.

In the United States, New Forests manages five mitigation banks, which are authorized under the federal Clean Water Act, through our joint venture in The Eco Products Fund, LP. These mitigation banks restore and protect wetlands and stream resources and are authorized to sell credits for mitigation to developers who cause unavoidable environmental impacts. Our mitigation banking portfolio includes the second largest bank in the United States, which encompasses approximately 19,000 acres of wetlands and forestland in Texas. Other banks are located in the Mid-west and Atlantic seaboard.

Social Capital

New Forests conducts stakeholder engagement across a range of activities, including at the corporate level and for each of our investment strategies. As these strategies seek to add value through responsible and sustainable investment, we have engaged with a number of stakeholders to promote innovative and forward-thinking forestry and environmental investment opportunities. Some of these engagements are highlighted in the table below.

Social Capital: Stakeholder engagement processes for all forestry assets are part of efforts to achieve sustainable forest management certification.

Strategy	Stakeholder & Type of Engagement
Australia New Zealand Forestry	<p>E-NGOs – exploring areas of synergy for achieving land management outcomes for climate change mitigation and biodiversity</p> <p>Government agencies (local, regional, and federal) – promoting functional rules for the Carbon Farming Initiative; participating in stakeholder forums; partnering with a Catchment Management Authority for biodiversity funding and projects</p> <p>FSC Australia – participating in industry group to support development of an FSC Australian standard and promoting rationalization of guidance for Australian forestry</p> <p>Property managers – offering training sessions on our approach to ESG management</p> <p>Local communities – stakeholder engagement plans elaborated as part of FSC certification process</p> <p>Agricultural interests – membership in Victorian and Western Australian Farmers Federations</p>
Tropical Asia Forestry	<p>FSC International – contributing to dialogue on standards and indicators; promoting biodiversity offsetting for previous conversion of forest</p> <p>Roundtable on Sustainable Palm Oil – promoting compensatory mitigation for biodiversity impacts and engaging with palm oil supply chain companies to address wildlife impacts</p> <p>Business & Biodiversity Offsetting Programme – staff participation in advisory board</p> <p>Government – promoting institutional frameworks to support institutional investment in forestry; promoting compensatory mitigation for biodiversity impacts</p>
Environmental Markets	<p>National Mitigation Banking Association – participating in industry events and lobbying efforts related to promote mitigation banking</p> <p>Army Corps of Engineers – outreach related to promotion of mitigation banking as preferred compensatory mitigation and future mitigation needs</p> <p>California Air Resources Board – promoting responsible and commercial carbon offset policies under California’s emissions trading scheme</p> <p>E-NGOs - collaborating on offset scheme and rule design recommendations for California’s emissions trading scheme and other carbon offset programs</p> <p>Land conservation organizations – relationship building to support land trust goals and investment opportunities</p> <p>Corporations and business (e.g. oil and gas, utility companies) – coordination on carbon offset policy recommendations and comments to regulators</p>

Contact

We welcome any feedback or questions you may have about this report or New Forests. For further information, please visit our website (www.newforests.com.au) or contact MaryKate Hanlon at mhanlon@newforests.com.au.