ASIA INVESTOR GROUP ON CLIMATE CHANGE

Asian Utilities Engagement Program

2021-2022 Progress Report

July 2022

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Executive Summary

AIGCC launched the Asian Utilities Engagement Program (AUEP), a collaborative engagement initiative between investors and electric utilities, in June 2021. The program was formed to increase the effectiveness of climate engagement with focus companies through a common agenda, and collaborative effort with consistent, long-term shared objectives to send a powerful signal that investors are asking for and expect companies to respond to climate change. The initiative complements and runs in parallel with the global Climate Action 100+ initiative.

At launch, the AUEP was supported by 13 investors with combined assets under management or advice of $US 8.8 trillion, engaging with five focus companies based in four different Asian countries. The common engagement agenda was set to focus on governance, decarbonisation strategies with coal and gas phase out timelines, disclosures, physical risks and public policy engagement.

Investor engagement with Asian electric utilities will play a key role in addressing climate risk as the sector contributes approximately 23 per cent of global greenhouse gas emissions and has a young asset age profile of about 13 years (versus an average economic lifetime of 40 years). This sector will also play a critical role in enabling the transition and decarbonisation of other sectors which are dependent on utilities.

Engagements to date have been progressing well, and we were encouraged to see a 2050 net zero commitment from focus company CLP in particular, with a commitment to phase out coal by 2040. There were also aspirational net zero ambitions set, such as Tenaga Nasional Berhad's 2050 and PLN's 2060 targets.

At the one-year mark, we are pleased to announce that three additional investors are joining the program, taking the combined assets under management or advice by the participating investors to $US 10 trillion. Two new focus companies have been added: PT Perusahaan Listrik Negara (Persero) (PLN) and Huaneng Power International. Indonesia will be an important focus country going forward as it works towards a just transition away from coal as currently, 14GW of coal-fired power is still expected to come online before 2030. The focus must now shift to implementation and a comprehensive approach to financing a just transition away from fossil fuels.

This report will discuss some of the key issues facing the Asian utilities sector and some high level reporting of the engagement progress to date with the five focus companies. We look forward to further engaging with all stakeholders in Asia's energy transition in the coming years.

2022 AIGCC Asia Utilities Engagement Program at a glance

16
Participants

7
Focus Companies

$10t
AUM of participants (USD)

5
Markets

The Asia Electric Utilities Sector

The Backdrop

The focus on climate change has only grown over the past year: the recent Working Group III report of the Intergovernmental Panel on Climate Change's (IPCC) Sixth Assessment Report (AR6) shows that keeping warming under 1.5°C will require greenhouse gas emissions to peak by 2025 at the latest, and be reduced by 43% by 2030. The IPCC is also clear that there is no conceivable path for achieving these reductions without a rapid transition away from fossil fuels. In the lead up to and during COP26 there was a positive step towards change in several Asian governments' climate policies including enhanced Nationally Determined Contributions (NDCs) under the Paris Agreement, as well as commitments to carbon neutrality.

The landscape for finance has also continued to evolve with the formation of various net zero alliances, including for asset owners and managers, as well as the Glasgow Financial Alliance for Net Zero (GFANZ) that is a collaboration of all the net zero alliances across the entire finance industry, committed to accelerating the decarbonisation of the global economy. Stakeholder demand for investors to act on cutting emissions through engagement with portfolio companies has never been stronger. It is with this backdrop that investors engage with focus companies to step up ambition and action on climate change.

Asian electric utilities have been dedicating increased resources to decarbonisation strategies. We were encouraged to see a 2050 net zero commitment from focus company CLP in particular, with a commitment to phase out coal by 2040. There were also aspirational net zero ambitions set, such as Tenaga Nasional Berhad's 2050 and PLN's 2060 targets. The focus must now shift to implementation and a comprehensive approach to financing a just transition away from fossil fuels.

Key topics of engagement

Energy security

Impacts of the Russia-Ukraine conflict on energy security are globally felt- whilst there is a desire for immediate relief to address the supply gap in certain parts of Europe, which have been heavily reliant on Russia's resources, there has been a clear reinforcement of the medium and long term need to rapidly accelerate the sustainable energy transition towards green technology and renewable energy resources.

Global energy prices will likely remain high and volatile in the near term with specific implications for Asia's importing nations. In the very short term, we have seen a switch back to coal as well as a renewed focus on LNG in some nations, such as Japan. However, we believe that these moves will only increase a nation's reliability on fossil fuel resources in the long run and reduce energy security. The key takeaway is that current energy systems are not fit for purpose and that renewable energy supply is necessary to protect against commodity pricing volatilities in fossil fuels, especially since renewable energy costs have decreased over time. To that end, several European nations, and Germany in particular, have already announced an acceleration of their renewable energy transition.

Technology

Carbon capture, utilisation and storage (CCUS)

Technology plays a crucial role for energy systems to reach net zero. According to the International Energy Agency (IEA), CCUS involves the capture of carbon dioxide (CO_2) from fuel combustion or industrial processes, the transport of this CO_2 via ship or pipeline, and either its use as a resource to create valuable products or services or its permanent storage deep underground in geological formations.

Large-scale adoption of CCUS continues to be a key assumption underlying many decarbonisation pathways, with projected CCS capacity requirements that are an order of magnitude greater than present capacity. Whilst the concept has been around for decades, CCUS is still facing significant challenges such as environmental risks, technical challenges, a lack of available financing, societal opposition, and policy uncertainty. In a report published by AIGCC in 2021, Wood Mackenzie found that significant cost competitiveness challenges for CCUS deployment in the electric utilities sector remains as late as 2040 as renewable energy, storage and other alternatives continue to fall in price. As companies set out decarbonisation strategies, capital allocation into different technologies need to take this context into account.

Ammonia co-firing

The use of ammonia as a fuel for fossil fuel power plants, widely known as ammonia co-firing with coal, is also a technology put forward as an additional tool for decarbonising the power sector in Japan. Ammonia, a derivative of hydrogen, is often applauded as a low-carbon fuel because the combustion of ammonia does not emit any carbon dioxide. However, if ammonia is produced from fossil fuels, CO_2 will be emitted during production process with limited overall emissions reductions on a life cycle basis. Other concerns remain on the high costs, other environmental impacts and the fact that Japanese utilities' reliance on this technology for decarbonisation will result in insufficient emissions reduction this decade and delays in coal phaseout. Reports by TransitionZero, Kiko Network and Climate Integrate discuss these issues in further detail.

Early Coal Phase Out and Just Transition

Due to the young age of the coal fleet in Asia, early retirement of coal assets in a transition to renewables is a focus for multiple stakeholders. In order to meet national net zero commitments, coal cannot continue to be a key incremental source to meet power consumption growth. The Asia Development Bank is working with regional and international partners to support and pilot a scalable Energy Transition Mechanism whilst other parties are also working on smaller scale private transactions to the same end. In both instances, just transition forms an integral part of the solutions. In addition, further work into transition and blended finance is underway with financing or enabling the accelerated, managed phaseout of high-emitting physical assets being a key focus of GFANZ that will aid in legitimizing these transactions and frameworks. High integrity carbon trading will also be needed to ensure packages are comprehensive.

Access to the Grid and Curtailment as a barrier

Grid connectivity and curtailment is still an issue faced by renewable energy generators in multiple Asian countries. Curtailment is where an electricity generating system is forced to stop exporting power to the grid or even temporarily shut down on instructions of the grid regulator, effectively wasting energy that has or could have been generated.

There are a few unique factors that make energy transition challenges on power grids even more significant for Asia Pacific countries: robust demand growth, a lack of generation and demand flexibility and the lower maturity of the power market structure. Investments in long distance, robust power lines and energy storage systems will be required, with each country also having its own set of challenges in terms of regulations as well.

Focus companies

China Resources Power

Name: China Resources Power Holdings Company Limited (CRP)

Country: China

Installed capacity: 43.4 GW (2020)

Coal capacity: 31.9 GW (2020)

The engagement group had a positive start with CRP to start the dialogue and to better understand CRP's decarbonisation strategy within the context of China's 3060 journey [1] . In particular, the company worked with investors on disclosures where a smaller group shared global best practice.

During the year, CRP announced plans for a spin-off listing of its renewable assets to raise funds for capital expenditure. Going forward, the group may not be engaging with the company to the same extent due to changes in investor holdings. However, CRP will remain under active monitoring within AUEP with a priority next step for the company to set interim milestones in the context of its longer term decarbonisation strategy.

1. The country is committed to hit peak emissions by 2030 and carbon neutrality by 2060.

CLP Group

Name: CLP Holdings Limited

Country: Hong Kong, China

Installed capacity: 20.8 GW (2020)

Coal capacity: 10.9 GW (2020)

The engagement group for CLP has been very active over the last year undertaking multiple meetings with the company. The lead investors, BNP Paribas Asset Management and Manulife Investment Management, also held one-on-one meetings with the company to discuss specific issues.

The group discussed investor expectations with the company of a 2040 coal phase out and net zero by 2050, key asks of the AUEP. We were encouraged to see these reflected in CLP's updated targets announced in September 2021. CLP also published its inaugural, standalone 2021 Climate-related Disclosures Report aligned with both the TCFD recommendations and the International Sustainability Standards Board (ISSB) prototype, making it one of the leading examples for disclosures, as the prototype was only released in November 2021. CLP also acknowledged the increasing demands for climate-related information by investor groups, including AIGCC, in its report.

Investors look forward to engaging with CLP on the roll out of their net zero plan as well as other aspects of their strategy such as physical risks and the potential for an earlier coal exit by 2030 for their Australia operations via EnergyAustralia.

Chubu Electric

Name: Chubu Electric Power Co., Inc. (Chubu Electric)

Country: Japan

Installed capacity: 77.9 GW (2020)

Coal capacity: 8.0 GW (2020)

Chubu Electric has been receptive to dialogue with AUEP's engagement leads since the AUEP was launched. On top of the key main asks of the program, the engagement group discussed topics related to the role of nuclear power within Japan's energy mix, the impact of carbon pricing on the company's coal power generation assets and businesses, and the feasibility of new technologies such as hydrogen, ammonia co-firing, and CCUS.

Given that coal assets reside with JERA, the joint venture between Chubu Electric and TEPCO, the leads also discussed investors' concerns on disclosures and governance on climate change with management. Investors look forward to further engagements on capital allocation and exit roadmaps for domestic and overseas coal plants.

Both Chubu and TEPCO faced climate resolutions filed by third party NGOs to disclose asset resilience in line with a net zero by 2050 pathway in 2022.

The resolutions, however, were rejected in the shareholder meetings of both companies (19.9% support in the case of Chubu, 10% support in the case of TEPCO). Although the resolutions did not receive a two-thirds majority to be accepted, investors will continue engaging with the companies on key asks of our program.

J-POWER

Name: The Electric Power Development Co., Ltd. (J-POWER)

Country: Japan

Installed capacity: 24.9 GW (2020)

Coal capacity: 8.4 GW (2020)

The engagement group for J-POWER held multiple meetings with the company since the launch of AUEP. The group progressed from discussing the key asks of AUEP to specific investor expectations for the company, such as the necessity of Paris aligned short and medium-term targets and the extension of its decarbonisation strategy to international assets. The engagement group also highlighted the heavy emphasis on ammonia co-firing and CCUS in their current Blue Mission 2050 plan.

In May 2022, Amundi, the lead investor for this AUEP engagement, joined two other major institutional investors, Man Group and HSBC Asset Management, and the Australasian Centre for Corporate Responsibility (ACCR), to co-file a set of three shareholder proposals. The proposals called on the company to:

- Set short and medium-term science-based GHG emissions reduction targets, and disclose a business plan to achieve them
- Disclose annually assessment details of capital expenditure alignment with these targets
- Disclose how (if at all) its remuneration policies will incentivise progress against its targets

While the 26% support fell short, it is a meaningful signal to company management and board to recognize investor concerns on climate and the increasing expectations of a credible decarbonisation pathway. We look forward to further engagement with the company in the coming year.

Tenaga Nasional Berhad

Name: Tenaga Nasional Berhad

Country: Malaysia

Installed capacity: 15.5 GW (2020)

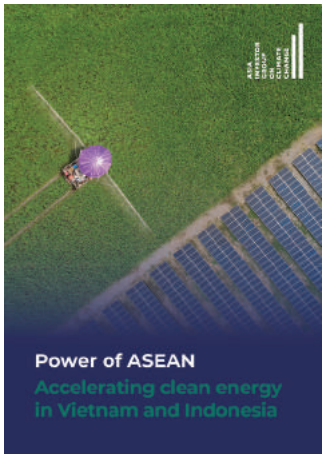
Coal capacity: 7.6 GW (2020)

The engagement group introduced the AUEP and the key asks of the program to the company, in particular, investor expectations of a 2040 coal phase out and net zero by 2050. Investors were encouraged to see the company subsequently announced its aspiration to achieve net zero by 2050 and upgraded targets, with commitment to reduce 35% of its emissions intensity as well as 50% of its coal generation capacity by 2035.

In early 2022, with Tenaga now focused on implementation and the refinement of targets, the engagement group met with the company's internal team responsible for setting out the sustainability pathway to provide input on best practice and investor expectations. Other points of discussion included raising ambitions further in the context of Malaysia's national policy and existing power purchase agreements (PPAs), with policy engagement a necessary part of the process.

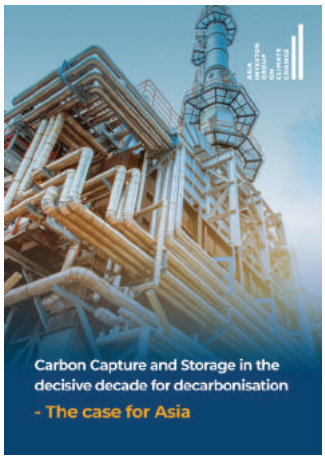
Outside of the company engagements

AIGCC Publications



Power of ASEAN – Accelerating clean energy in Vietnam and Indonesia

Published by AIGCC in October 2021, this report takes a deep dive into the power sectors of Vietnam and Indonesia and simulates alternative power capacity and generation mix scenarios to current Power Development Plans (PDPs). The report found that higher solar and wind penetration can lower the average system cost in both countries, whilst meeting demand growth. The stability of power supply is also not compromised under this scenario. The report also explores the multiple barriers for the economic entry of solar and wind capacity in the ASEAN bloc. Read full report



Carbon Capture and Storage in the decisive decade for decarbonisation – The case for Asia

In December 2021, AIGCC published a report focused on CCS in Asia, particularly in the four key markets of China, India, Japan and South Korea. As large-scale adoption of CCS continues to be a key assumption underlying major decarbonisation pathways as a means to bridge the emissions gap, this report aims to validate whether such CCS capacity projections for 2050 are plausible in the Asian context. This report covers two main areas: a) Analysis by Wood Mackenzie to assess the drivers of CCS feasibility, consisting of cost competitiveness to alternatives, policy and regulatory support and storage availability, to assess the competitiveness of CCS in the power generation and steel sectors of China, India, Japan, and South Korea, and b) AIGCC's further research into additional obstacles to large-scale implementation of CCS. Read full report

Policy engagements

Policy engagement under the AUEP was primarily targeted at the issues of increasing renewable energy in the power sector and early coal phaseout. The engagement involved raising awareness and understanding of relevant new research on these topics that would help in policy planning on energy transition.

Within a month of the Program's launch, AIGCC convened a joint webinar with the Japan Energy Transition Initiative (JETI) in July 2021, and brought together senior leaders from business, finance, policymaking and think tanks to discuss issues and solutions towards driving innovation in policy towards reducing greenhouse gas emissions. Collaboration between the power sector and the government will be key to Japan meeting its net zero targets. The seminar featured Sumitomo Mitsui Trust Asset Management, one of the investors involved in the Asian Utilities Engagement Program. A video recording of the webinar is available here.

In May 2022, AIGCC held another similar event on the theme of Japan's energy transition on the sidelines of Responsible Investor Japan 2022, bringing in experts such as Professor Frank Jotzo, Dr. Kimiko Hirata and Professor Hiroshi Takahashi. The event focused on the role of renewable energy and ammonia co-firing in Japan's Clean Energy Strategy that is slated for release later in the year. A video recording of the general event is available here.

The general session was followed by a closed-door roundtable that brought together representatives from key government bodies responsible for formulating policies on energy transition, domestic and international investors, and corporate groups. The discussions pertained to the need for a step up in the supply of renewable energy in Japan's energy mix over the coming decade to cater to companies that have committed to RE100 targets and for Japan to remain competitive as an investment destination. The role that ammonia co-firing would play in Japan's energy transition was also discussed, specifically distinguishing green ammonia from other forms generated from fossil fuels. A similar engagement is currently being planned for Malaysia.

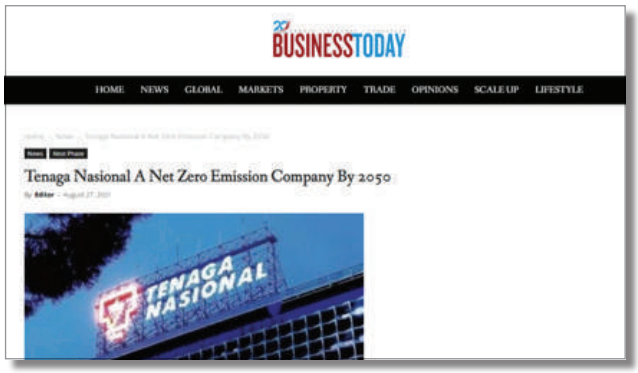
AIGCC is also engaging in the ASEAN Taxonomy consultation process that is being organized by the ASEAN Taxonomy Board, with a particular focus on the power sector.

AIGCC's official 'side event' to Responsible Investor Japan 2022 on 26 May 2022

Media coverage

In the last 12 months, the Asian Utilities Engagement Program garnered over 220 mentions in top global media. Leading international financial news organisations, such as The Financial Times and Euromoney have reported on the Program following its launch, with Euromoney stating that engaging with Asian electrical utilities are "key to net zero". Other notable media coverage include Eco-Business, The Straits Times, South China Morning Post, and The Asset, which are prominent news sources and trade publications for sustainability-related updates in the region.

When focus companies in the Program announced their net zero pledges, these too caught significant international and regional media interest. For example, CLP's pledge to commit to net zero by 2050 and its plans to accelerate phase out coal-fired generation by 2040 was reported extensively in South China Morning Post and Euromoney, while Tenaga's pledge to commit to a net zero carbon emission company by 2050 was reported by Business Today.



2022: The journey continues

All investor engagements will be taking place in the context of a diverse region and the recognition that each country has its own nuanced decarbonisation pathway, while also acknowledging the science and global action that are required. AIGCC looks forward to supporting further work on sector and regional pathways in collaboration with investors and other stakeholders. The issues of a just transition will also increasingly come to the forefront as the Just Energy Transition Partnerships come to Asia: cooperation schemes between multiple stakeholders that are intended to activate private and public financing on a large scale for specific investments, such as a socially just coal phase-out.

In the coming year, investors look forward to stepping up engagement with high emissions sectors, and Asian utilities will continue to be in focus. Asia currently makes up 50% of global GHG emissions and efforts to decarbonise utilities in the region are critical to reaching global climate goals as well as reducing pollution and ensuring the health and well-being in local economies. AUEP will be adding two additional focus companies and one new jurisdiction, Indonesia, with three additional participating investors. AIGCC will continue to facilitate policy engagement opportunities for investors on these issues as well in the coming years. In the next few months, AIGCC is partnering with the G20 Energy Transition Working Group and a few other partner organisations to host a workshop in Jakarta on unlocking finance to accelerate a just energy transition in emerging economies.

Investors will continue to push for faster and more ambitious climate commitments from focus companies. We also look forward to seeing more companies' climate transition plans and how they provide regular and transparent disclosure against the TCFD reporting framework on all of their activities to assess continued progress, particularly on: governance, decarbonisation strategies, physical risks and policy advocacy. Investors' focus has now shifted to implementation and how company net zero goals will be met, with short, medium- and long-term emissions reduction aligned with the Paris Agreement.

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