A FUTURE WITHOUT COAL

Banking on Asia's Just Energy Transition

EXECUTIVE SUMMARY

About this report

This report, commissioned by Fair Finance Asia, analyzes how financial institutions operating in Asia can contribute to a just energy transition.

About Fair Finance Asia

Fair Finance Asia (FFA) is a regional network of civil society organizations (CSOs) committed to ensuring that financial institutions operating in Asia respect and uphold the rights and social and environmental well-being of local communities.

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Editorial Review & Contributions

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SUMMARY & HIGHLIGHTS

Coal accounts for 74% of all electricity produced in India, 66% in China, 59% in Indonesia, 52% in the Philippines, 47% in Vietnam and between 1% and 45% in the other eight Asian countries covered in this study.

Continued use of thermal coal is the number one cause of global temperature rise. It is responsible for nearly half of carbon dioxide emissions worldwide and 72% of greenhouse gas (GHG) emissions from the energy sector. A new report by the Intergovernmental Panel on Climate Change (IPCC) released in August 2021 issued a "code red" for the world, warning that without deep and immediate cuts to carbon pollution, the 1.5°C goal of the Paris Agreement "will quickly fall out of reach."

A vision of a different energy future is urgently needed. Yet, across Asia, coal consumption has doubled in the last decade. Coal accounts for 74% of all electricity produced in India, 66% in China, 59% in Indonesia, 52% in the Philippines, 47% in Vietnam and between 1% and 45% in the other eight Asian countries covered in this study. Together, these 13 countries[i] are developing coal-fired power projects with a total capacity of 432 GW which, when complete, will increase their coal-fired power capacity by 30%.

Social and Environmental Impacts of Coal

Coal is a major contributor to climate change, causing higher temperatures, droughts, floods and extreme weather patterns.

For the majority of Asia's population, these have serious consequences for housing, livelihoods, health and food security. Coal combustion also causes significant air pollution from the release of nitrogen oxides, sulfur dioxide, particulate matter and heavy metals, while coal mining and combustion cause water pollution and consume large volumes of water.

The air pollutants emitted by coal-fired power plants are harmful to human health and a major cause of respiratory and cardiovascular disease. The contamination of water, air and soil by coal combustion threatens the food security of vulnerable communities due to adverse impacts on crop productivity, fish and life in rivers and biodiversity. Land grabbing by coal companies has led to rural communities and Indigenous peoples losing agricultural and traditional lands. Coal mine workers labor in dangerous working conditions for low wages, and poor health and safety standards have resulted in high rates of death and injury.

[i] FFA countries: Cambodia, India, Indonesia, Japan, Pakistan, Philippines, Thailand and Vietnam. Non-FFA countries: Bangladesh, China, Malaysia, Singapore and South Korea.

Policies to Limit the Use and Impact of Coal in Asia

To meet their obligations under the Paris Agreement, many Asian countries are taking steps to limit the negative climate impacts of coal.

Indonesia, Pakistan, Philippines, Singapore and South Korea have all introduced policies to stop new coal-fired power plant projects. The adoption of carbon capture and storage (CCS) technology to improve the efficiency of coal-fired power plants has become a policy focus in China, Japan and South Korea. Several countries have also committed to introduce a carbon tax, including India, Japan, Singapore, South Korea and Vietnam.

However, these policies are not sufficient to phase out coal and achieve the Paris Agreement commitments. Although fewer coal-fired power plants are being constructed, those already in operation and under development will continue to operate for the next 35 to 40 years. Meanwhile, some Asian countries are switching away from coal to other fossil fuels (such as natural gas) that will continue to emit GHGs. Efforts to make coal-fired power plants more efficient will have very little impact on reducing GHG emissions, and new market mechanisms like carbon taxes and incentives to stop investments in coal will not be fully effective in turning the tide.

Coal Financing in Asia

Continued growth in Asia's coal sector is largely due to available funding coming from banks and investors. In the past five years (2016–2020), banks operating in Asia have provided USD 683 billion in loans and underwriting services to companies active in coal mining and coal-fired power in Asia.

Annual credit flows to coal peaked in 2018 and have since showed a modest decline (-16% in 2020). Most loans and underwriting services were provided to coal companies active in China, followed by coal companies in Indonesia, Japan and India. Chinese banks accounted for two-thirds of the loans, followed by banks from Japan, India and South Korea. Banks from outside the region (United Kingdom, United States, France and other countries) made only a minor contribution to total loans and underwriting services.

In June 2021, investors held USD 70.4 billion in bonds and shares issued by companies active in coal mining and coal-fired power in Asia, 86% of which were in the form of shares. The value of the shares of Asian coal companies owned by institutional investors peaked at the end of 2017 and declined by 28% by mid-2021. A comparison of baseline investments and actual investment value (i.e. whether the portfolio composition had stayed the same) shows that approximately USD 10 billion more investments were made in the peak period of 2017–2019. The difference between baseline and actual investments since the fourth quarter of 2020 is smaller, but still indicates an overall increase in fossil fuel investments.

Most investments are currently made in the shares and bonds of coal companies in India, followed by companies in China, Japan and Malaysia. Investors from the US accounted for 20% of total bonds and shareholdings, and investors from Japan, China and India also held significant stakes. The biggest investors in the Asian coal sector are Japan's Government Pension Investment Fund, India's Life Insurance Corporation, US asset managers BlackRock and Vanguard and Malaysian investors Khazanah Nasional, PNB and EPF.

Towards a Just Energy Transition

The enormous impacts of coal on climate change, the environment and society must be urgently addressed. However, simply replacing coal with renewable energy is not a straightforward solution to the social and environmental injustices of the global energy system. Instead, Asian civil society movements are calling for a "just energy transition" based on the following principles:

- No financing for new coal projects for electricity generation and phasing out existing coal-based power generation;
- Development of a time-bound transition away from other fossil fuels for electricity generation;
- Active investment in renewable energy generation;
- Long-term planning and strategies to mitigate the adverse environmental and social impacts of renewables;
- Respect for land rights and Free, Prior and Informed Consent (FPIC), and clear policies for community participation, gender sensitivity and consultation with civil society organizations (CSOs) in large energy projects;
- Protection of the rights of workers and mainstreaming of Human Rights Due Diligence (HRDD) during the energy transition;
- Safeguarding the health, livelihoods, culture and heritage of communities impacted by the continued use of fossil fuels;
- Active and meaningful engagement and participation of women in the energy transition; and
- Investments in access to electricity for all.

Realizing a just transition in Asia will require financial institutions to play a pivotal role, but success will also largely depend on governments promoting and regulating a shift from fossil fuels to renewable energy in a manner that safeguards the environment and respects human rights.

Risks and Opportunities of the Energy Transition

There are strong monetary arguments for financial institutions in Asia and around the world to transition from coal to renewables.

Divesting from coal would not only allow them to avoid the mounting financial risks of coal, but also capitalize on the financial returns offered by increasingly profitable renewable energy investments.

This transition to renewable energy is inevitable. Between 2016 and 2020, renewables outpaced coal in four important areas: revenue growth, EBITDA (Earnings Before Interest, Tax, Depreciation and Amortization) growth, return on capital employed (ROCE) and value growth. Under the International Energy Agency's (IEA) 1.5ºC scenario, policy responses by governments, shifts in the supply chain and changing attitudes of financiers will all tilt in favor of renewable-related assets.

Investors in coal-related assets might see a strong decline in the value of their shares and a significant devaluation of their bond values. Banks might lose 76% of their loan value. Meanwhile, shareholders of renewable-related assets could benefit from value growth and debt with a much lower default risk than the debt of coal-related companies.

Role of the Financial Sector in the Energy Transition

The financial sector has a crucial role to play in a just energy transition in Asia. Despite commendable efforts to promote sustainable finance at the global level (NGFS and SBN), the regional level (ASEAN+3) and in various Asian countries (China, Singapore, Malaysia, Indonesia and Vietnam), financial institutions in Asia continue to finance coal on a large scale and are relatively less interested in renewable energy financing. There are three main reasons for this:

- The absence of a financial regulatory framework to incentivize Asian financial institutions to finance the transition. Both banks and regulators focus on short-term risks and do not fully appreciate how environmental, social and governance (ESG) risks can become financial risks.
- Large energy companies in Asia are not developing large renewable energy projects, and financial institutions are not interested in financing smaller renewable energy projects by start-ups and small and medium-sized enterprises (SMEs).
- Asian governments are not investing in electricity transport infrastructure, which would make it easier for renewable energy projects to develop and attract financing.

However, a shift is underway, prompted primarily by the commitments of three countries – China, Japan and South Korea – to achieve net-zero GHG emission plans. Financial institutions are expected to follow suit, and banks in Taiwan and Vietnam have begun to show more interest in financing renewables. China has also committed to stop financing coal projects overseas.

Financial regulators and central banks have a major role to play in catalyzing these developments and motivating banks to finance the transition from coal to renewable energy. This can be done by structuring debt relief from foreign creditors; bringing banks together and reaching consensus on where to invest; and focusing central bank asset purchases on green bonds.

RECOMMENDATIONS

Based on the findings of this study, Fair Finance Asia (FFA) has developed the following recommendations for financial institutions, Asian governments and CSOs. These recommendations are intended to motivate key actors and leaders to facilitate and finance the shift from coal and other fossil fuels to renewable energy, and ensure a just transition.

Recommendation for CSOs

CSOs should engage with financial institutions and governments through all available avenues of influence to ensure they implement the recommendations listed here.

CSOs should actively engage in the key processes of financial institutions, such as providing evidence-based inputs at annual general meetings and taking advantage of opportunities to comment on the policies of financial institutions.

CSOs should engage with multilateral financial institutions (MFIs) to influence their environmental and social policies, as MFIs have the potential to shape both country-level policies and those of national financial institutions.

CSOs should build their capacity to track how new climate monitoring tools are being used in the financial sector and to respond to claims made by financial institutions about their alignment with the Paris Agreement.

CSOs should concentrate on monitoring the climate impacts of sectors responsible for the bulk of global GHG emissions (fossil fuels, agriculture and forestry). A focus on measurable, non-Paris-aligned corporate activities rather than (financed) GHG emissions would be more efficient, easier to communicate and allow CSOs to influence financial institutions more effectively.

Global civil society must work together to track the cross-border financing of key sectors (fossil fuels, agriculture and forestry) and create platforms for sharing data, knowledge and experiences across the region to uphold the duty of care of financial institutions, for instance, through litigation.

CSOs should raise more awareness of issues related to the just and sustainable energy transition and educate citizens and consumers about their individual responsibilities.

CSOs should build their capacity to monitor the policies of financial institutions that affect lending and investment decisions, as the capacity to monitor government regulations and businesses, including financial institutions, is key to meeting timelines and targets for a just transition. The Fair Finance Guide International Methodology (FFGI methodology) is a comprehensive and rigorous assessment tool that CSOs can use.

Recommendations For Financial Institutions

- Financial institutions should have a clear and detailed strategy to address the climate impacts of the activities and companies they finance and invest in. Financed companies need to be aligned with a 1.5° C scenario based on science-based targets that cover Scope 3 emissions. The climate impact of financial institutions needs to be reduced to zero by 2050 at the latest and halved by 2030 at the latest.

- Leaders of financial institutions should make urgent strategic changes to ensure their loans and underwriting services directly support climate mitigation, environmental resilience and respect for human rights and labor rights in Asia.

- During the lending process, financial institutions should actively engage with potential borrowers to request and obtain all necessary information on the potential negative impacts of their activities on sustainability, and make financing agreements conditional on averting or addressing negative impacts swiftly.

- Financial institutions should ensure their climate strategy is reported transparently and the verification and monitoring of their climate impacts are credible. They should also contribute to the development of climate monitoring tools to support more reliable and robust reporting in the financial sector with greater sector coverage and alignment with a 1.5ºC scenario.

- Since it is not yet mandatory for financial institutions to disclose and audit their GHG emissions, they should voluntarily make their financing, investment portfolios and climate impact assessments more transparent. This would allow auditors, researchers, CSOs, media and other stakeholders to monitor and independently assess the Paris alignment of financial institutions.

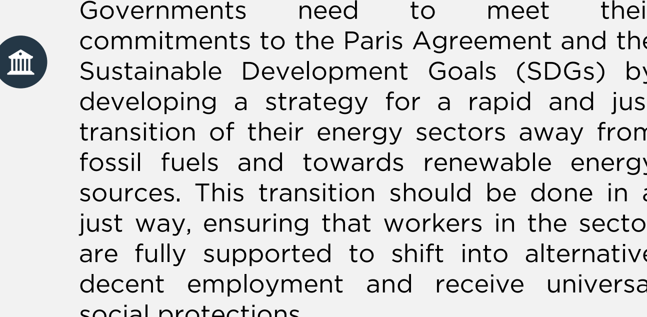
- Financial institutions should develop their climate change strategies into sectoral policies and strategies, especially for high-impact sectors like fossil fuel, including the coal industry. Financial institutions should stop funding coal as soon as possible and actively seek opportunities to expand renewable energy generation in Asia.

Recommendations For Financial Institutions

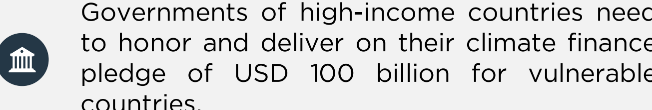
Financial institutions should recognize that the transition from coal and other fossil fuels to renewables in Asia needs to be a just transition. Financial institutions should therefore commit to the following principles and demand that the companies they finance and invest in do the same:

- End financing for new coal projects for electricity generation and adopt a phased approach to move away from existing coal-based power generation.
- Ensure that coal is not replaced by other fossil fuels, such as natural gas, and that other fossil fuels are phased out from electricity generation on a publicly disclosed timeline.
- Invest actively in renewable energy generation.
- Engage in long-term planning for the transition and ensure strategies are in place to mitigate any adverse environmental and social impacts of renewables.
- Ensure that land rights and Free, Prior and Informed Consent (FPIC) are respected, and there are clear policies to mainstream community participation, gender sensitivity and CSO consultations in the development of large energy projects.
- Protect the rights of workers at project sites and mainstream Human Rights Due Diligence (HRDD) as part of the process.
- Safeguard the health and livelihoods of workers and the culture and heritage of communities.
- Ensure the active and meaningful participation of women in the energy transition.
- Invest in access to electricity for all.

RECOMMENDATIONS FOR ASIAN GOVERNMENTS AND THE ASEAN



Governments need to meet their commitments to the Paris Agreement and the Sustainable Development Goals (SDGs) by developing a strategy for a rapid and just transition of their energy sectors away from fossil fuels and towards renewable energy sources. This transition should be done in a just way, ensuring that workers in the sector are fully supported to shift into alternative decent employment and receive universal social protections.



Governments of high-income countries need to honor and deliver on their climate finance pledge of USD 100 billion for vulnerable countries.

Governments should create a level playing field for banks in the form of mandatory regulatory or legally binding minimum requirements to avoid free riders. These need to strengthen banks' ESG risk and impact assessment methods while also defining and promoting lending for socially and environmentally sustainable activities, and phasing out lending that is not aligned with the Paris climate goals and the SDGs. These include mandatory and audited carbon emissions disclosures by companies and the financial institutions that finance them based on the Greenhouse Gas (GHG) Protocol and existing climate-monitoring tools for financial institutions.

In line with their commitment to make **"finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development"** (Paris Agreement, Article 2.1(c)), governments should establish a financial regulatory framework to incentivize Asian financial institutions to become Paris-aligned and finance a rapid and just transition of their energy sectors away from fossil fuels towards renewable energy sources. This can be achieved, in part, by developing an ambitious energy transition plan; creating a fiscal space by structuring debt relief from foreign creditors; bringing banks together to create consensus on where to invest; and focusing asset purchases on green bonds.

Governments should invest in infrastructure to transport electricity across their countries. This could make it easier for smaller and start-up companies to invest in renewable energy generation, and it would also increase access to electricity for local communities.

Governments should put sufficient regulations in place to ensure that all companies, in the energy sector and beyond, live up to the expectations of the United Nations Guiding Principles on Business and Human Rights (UNGPs). These regulations need to be implemented and monitored properly to ensure that companies respect human rights and provide access to remedy.

A carbon tax can be a useful policy instrument to promote the transition from fossil fuels to renewables. For a carbon tax to be effective, governments should:

- be transparent about revenues and expenditures;
- ensure that the tax influences polluting behavior effectively; and
- reinvest revenues in improving access to renewable energy for local communities.

Governments should include climate change in school and university curricula and ensure that academic and professional training on the energy transition is made available.

Governments should finance research and consumer education on what a just energy transition means and how it can be achieved in the Asian context.

Governments should promote and provide financial support for community-led renewable energy projects.

Governments should provide inclusive and fair compensation schemes for communities negatively impacted by (renewable) energy projects.

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