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ANZ FY22 Full Year Results

Climate Finance Assessment

In this first in CEF's series of climate finance analyses of Australia's Big 5 banks – ANZ, CBA, Westpac, NAB and Macquarie Bank – we review ANZ's efforts against four criteria that are key to assessing progress on decarbonisation in line with science-based targets.

Globally, CEF estimates that more than US$100 trillion is required to fund global energy systems and decarbonisation by 2050,[1] and Australia's banks play a decisive role in whether we achieve the scale and pace of this capital flow here in this crucial decade to 2030. ANZ is moving in the right direction on climate, yet there is still a long way to go in matching the ambition required nationally, to meet the Paris Agreement goals.

Momentum in Australia is accelerating with recent movements such as the legislation of a 43% decarbonisation by 2030 target[2], net-zero announcements by corporate leaders[3], and a crackdown on greenwashing by APRA, ACCC & ASIC[4] all placing increased pressure on financial institutions to adapt and respond to a rapidly changing global landscape. Coupled with this, frameworks such as GFANZ[5], NGFS[6], SBTi[7] and the TCFD[8] are amplifying the need for improved transparency and globally consistent disclosures in the financial sector.

Financial institutions are facing an urgent accountability to align their financing decisions and financed emissions – i.e. the emissions of their customers – with a 1.5 degree warming limit. This involves both increased financing towards climate solutions, as well as winding down financing of high emitting customers and sectors, starting with those still building greenfield projects. With that in mind, ANZ's 2022 full year results have been assessed against four themes – ANZ's climate financing pledge, customer engagement, emissions intensity by sector, and its energy loan book.

1. Climate financing pledge

ANZ's $50bn Sustainable Finance (SF) Target[9]

ANZ's 2022 full year results reports progress to 1st half FY22 only

ANZ has achieved $31bn of their target to reach $50bn sustainable financing (SF) by 2025 since October 2019 – that's 62% of the target in just 2.5 years of the 2025 pledge. This year, ANZ funded and facilitated $10bn in 1HFY2022. At this rate, ANZ will hit $50bn by mid FY23

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[1] IEA, World Energy Investment 2022 and World Energy Outlook 2022
[2] Australian Government, Climate Change Bill 2022
[3] AFR, 'Businesses in a race to commit to net zero', 6 Oct 2022
[4] 'From culture to compliance: Regulators confirm focus on "greenwashing" and assessment of climate change risks', 22 Jun 2022 and 'Greenwashing: ASIC's guidance on how to avoid it', 17 Jun 2022
[5] Global Financial Alliance for Net-Zero
[6] Network for Greening the Financial System
[7] Science Based Targets initiative
[8] Task Force for Climate-related Financial Disclosures
[9] ANZ's target to fund and facilitate at least A$50 billion by 2025 towards helping their customers improve environmental sustainability, increase access to affordable housing and promote financial wellbeing

and go on to achieve some $80bn by 2025. Add to that strong sector growth – ANZ reports a 76% increase in the number of SF deals between this time last year – increased national decarbonisation ambition, greater state and federal policy certainty, and, therefore, increased size of investment opportunity, and the scope for ANZ to claim a greater share of the trillions of dollars necessary to build a carbon-free economy is ripening.[10] We would advocate ANZ make a new, more ambitious $100-200bn by 2030 pledge. This is a huge growing investment and lending opportunity for ANZ, and all the Australian financial institutions, as highlighted by Blackrock.[11]

Proportionally, 61% ($19bn) is funded via ANZ's balance sheet loans and other credit lines, and 39% ($12bn) are facilitated transactions through ANZ advisory services, ESG-format bonds, and loans initially underwritten by ANZ and subsequently sold on to other lenders. The funded portion of ANZ's SF target is up from 55% last year, which shows ANZ is claiming a greater portion of their SF target from direct capital allocation vs measuring their 'facilitation' of other financial institutions efforts.

This is important because these days, unlike in their SF reporting, we seldom see the banking sector report on their 'facilitation' of coal, oil and gas transactions, which underpins emissions expansion. Banks should report to the same level of transparency in high emission transactions – otherwise it is greenwash (investor deception by disclosure omission).

Digging deeper and we find that 40%[12] of ANZ's funded portion is allocated to environmental categories (energy, transport, green buildings, water, waste and environmental markets) – which translates to $7.6bn out of the $31bn financing to date – i.e. the current trajectory is 25% allocation towards environmental activities.

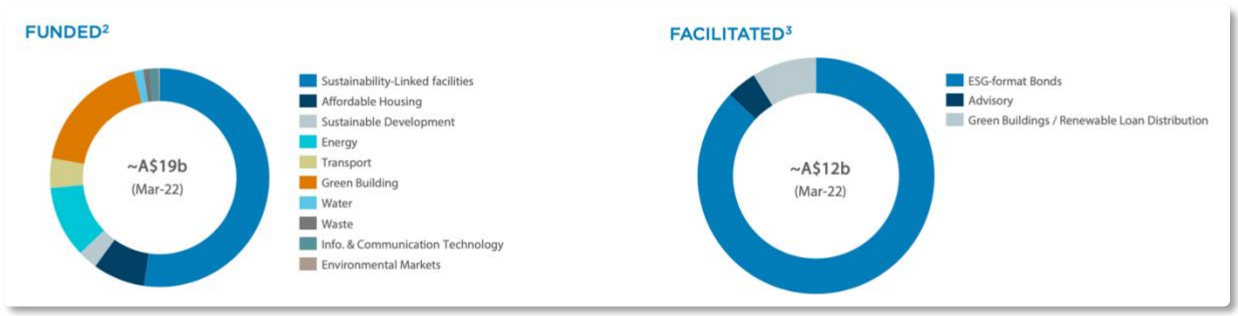

Figure 1 – ANZ 2022 ESG Investor Briefing, p.33

2. Customer engagement[13]

[10] AFR, 'ANZ's $50b a drop in ocean of sustainable finance: Elliott', 2 Dec 2020
[11] Business Insider, 'BlackRock CEO Larry Fink calls decarbonising economy the greatest investment opportunity of our lifetime', 19 Jan 2022
[12] ANZ's FY22 full year results haven't provided figures towards each category. 40% is a conservative estimate derived with consultation of ANZ's FY21 environmental classification plus this year's pie graph (figure 1)
[13] ANZ 2022 ESG Investor Briefing, p.31-32

ANZ's ambition is to be the leading Australia and New Zealand-based bank in supporting customers to transition to net zero emissions by 2050. Without a taxonomy defining what constitutes a Paris-aligned transition plan, the task of assessing and normalise corporate decarbonisation criteria across the banking sector is enormous, and ANZ shows greater transparency in this area than the other big Australian banks. In the near future, the Australian Sustainable Finance Institute (ASFI) taxonomy will establish a shared baseline to measure heavy emitting customers' progress to decarbonisation and provide transparency and assurance over transition plan assessments.[14]

Since 2019, ANZ has been engaging with 100 of their highest emitting customers – which together comprise ~30% of Australia's national emissions – to support them in establishing/strengthening their net zero transition plans. The 100 customers are split 40%:60%, Australia:NZ & International in terms of ANZ's exposure at default (EAD)[15]. Transition plans of the 100 companies are classified by ANZ into 4 categories ranging from (a) advanced, (b) developing/intermediate, (c) underdeveloped/starting out, (d) no public plans.

A key question to ask is what exactly constitutes an "advanced" transition plan according to ANZ, and whether ANZ's current classification is justifiable. ANZ considers that a "robust" or "advanced" low carbon transition plan will incorporate three key elements – Governance, Targets and Policies, and Disclosures – where Targets and Policies refers to "action to reduce greenhouse gas emissions, including public targets to support government policies up to 2030 in their key markets of operation **or** company policies or statements setting out long-term goals[16].

But the criterion specifying "2030 targets" or "long-term goals" is too loose and not Paris-aligned. We know that long-term emissions reduction targets must be coupled with interim targets, ensuring year-on-year sustained emissions reduction to align with the 1.5°C trajectory of the Paris Agreement. This area of reporting is at high risk of greenwash where the outcome of ANZ's customer engagement efforts is over-inflated, and undermines credible action. As CEO Shayne Elliot has argued, "What's also changing now is a much clearer focus around the work that needs to start now, what needs to be done in this decade, as opposed to just buying time and waiting for the long term".[17]

We would expect ANZ to rapidly tighten these category definitions, meaning ANZ's engagement success ratings will slip without significant ongoing customer improvements – and improvements are likely given the rapid convergence of policy and investment drivers including likely reforms to the Safeguard Mechanism, the federal government's 82%

[14] AFR, 'Transition rules speed up as emission target set', 8 Aug 2022
[15] Exposure at default (EAD) is the total value a bank is exposed to when a loan defaults.
[16] ANZ, 'Low-Carbon Transition Plans', 1 May 2019 and ANZ 2021 ESG Supplement, p.25. No further detail or conflicting evidence has been provided this year.
[17] AFR, 'Cost remains a challenge for burgeoning hydrogen industry', 9 Dec 2021

renewables by 2030 electricity target and commitment to the global methane pledge, and growing global investor pressures.

Additionally, the obvious and more challenging issue for ANZ is determining the impact of their high-emitting customers' upstream and downstream supply chain emissions – i.e. inclusive of scope 3 emissions. It seems highly unlikely that an Australian-based energy company, per ANZ's example[18], has a transition plan to turn down their operations in line with the Paris Agreement and the International Energy Agency's Roadmap to Net Zero by 2050, when Australia currently has 100 new fossil fuel projects under development nationally.[19] As the third largest fossil fuel exporting nation globally, this issue is an Australian economy wide threat, but we would call on ANZ to take a leadership role in acknowledging and informing public debate and action to a path aligned with the SBTi, inclusive of our huge export sectors. Rebuilding the banking sector's social licence to operate is a key board consideration.[20]

3. Sector emissions intensity[21]

ANZ's emissions intensity reporting currently covers large scale commercial real estate, including office buildings and shopping centres – both on track to meet the 2030 target – and power generation – not on track to meet 2030 target.

For the power sector, the Federal Government's new 82% decarbonisation by 2030 target means this is a sector needing urgent step-up in investments in firmed zero emissions generation and grid infrastructure – which means this is a priority sector for all the banks, with a particular focus towards leveraging the risk sharing of public-private partnerships in decarbonisation, as per funding allocations in the Federal Budget of October 2022 ($20bn Rewiring the Nation, $1.9bn Powering the Regions Fund, $15bn National Reconstruction Fund).[22]

ANZ reports they are setting targets for additional nine priority sectors by 2024, with pathways and targets for oil and gas and building products to be released before December this year. The real understated fact here is that none of these targets are science-based targets aligned with and verified by the SBTi.

4. Energy loan book

ANZ's thermal coal EAD is trending down with a 50% reduction on last year's balance, and is currently at $200m, a dramatic improvement given ANZ was the coal bank of Australia less than a decade ago. But the contrast is stark, oil and gas extraction EAD shot up by 19% this

[18] ANZ 2022 ESG Investor Briefing, p.32
[19] The Saturday Paper, 'How the government supports greenwashing', 29 Oct 2022
[20] Governance Institute of Australia, 'Social licence is key to Australian business survival', Jul 2018
[21] ANZ 2022 Full Year Results, p.70-73
[22] Climate Energy Finance, 'Federal budget: Substantial progress on energy transition, but fossil fuel tax reform a serious omission', 26 Oct 2022

year – ANZ cited currency fluctuations and increased lending to meet energy supply shortages as the reason for this.

At a $7bn balance, ANZ's oil and gas extraction balance sheet isn't representative given ANZ fails to disclose wider 'facilitation' in expanding the oil and gas sector. For example, a single transaction earlier this year – where ANZ, NAB and Westpac acted as 'mandated lead arranger and book runner' – facilitated capital worth AU$5.4bn to Global Infrastructure Partners' acquisition of a 49% stake in Woodside's Scarborough-Pluto gas project – a project which is estimated to produce 1.6bn tonnes of emissions over its lifetime.[23] This speaks to an urgent need for greater honesty in terms of transparency around corporate lending and other facilitative financing of long dated new projects in high emitting sectors.

ANZ promised, in 2020, to exit thermal coal by 2030 but is yet to make exit plans for the oil and gas sector – emissions intensity reduction targets will be out before December and to be meaningful they would be designed in consultation with SBTi best practice.

The IEA's World Energy Outlook (WEO) 2022 report released in October highlights for the first time the 80-90% reduction in oil, gas and coal emissions globally that is needed to align with a 1.5°C outcome.[24] World expectations for investing in alignment with a sustainable economy are moving rapidly and ANZ's leadership here is strategically important for Australia.

ANZ did not publish their renewable energy portfolio in this year's results, which means the latest data can only be found in ANZ's 2021 ESG Data Pack[25]. This is puzzling, as renewable energy exposure is key to a comprehensive analysis of ANZ's decarbonisation efforts. As at 30 Sep 2021, ANZ's renewables portfolio was at $1.4bn comprising 88% of their overall power generation financing, with gas at 9% and coal 3%. This $1.4bn EAD in renewables sits in stark comparison to the $6.5bn[26] EAD in coal/oil/gas (a ratio of 1:4 respectively). The bank needs to progressively and systematically reduce lending to high emissions sectors, as well show how it is seizing the massive and growing investment opportunities as Australia shifts to becoming a renewable energy and critical minerals superpower.

[23] Market Forces, 'Repeat offenders NAB, ANZ and Westpac bankrolling "bet against the Paris Agreement"', 18 Jan 2022
[24] IEA World Energy Outlook 2022
[25] ANZ 2021 ESG Data Pack
[26] Calculated from ANZ's 2021 EAD in oil and gas extraction, thermal coal, and coal and gas project finance.