CLIMATE ENERGY FINANCE

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CommBank (CBA) FY22 Full Year Results
Climate Finance Assessment

In the fourth in CEF's series of climate finance analyses of Australia's Big 5 banks, we review CommBank's FY2022 full year financial disclosures. We have published analyses of ANZ, NAB and Westpac. Macquarie Group Limited is forthcoming.

We assess against four material decarbonisation criteria for the banking sector – climate solutions financing, financed emissions reduction by sector, customer transition plan engagement, and trends in the bank's energy loanbook.

Pivoting the major banks' trillion dollar balance sheets towards climate solutions will be key to unlocking the $420 billion Australian decarbonisation opportunity. Global decarbonisation momentum plus key domestic policy shifts – the government's 43% emissions reduction target, 82% renewables target, $15bn National Reconstruction Fund, $1.9bn Powering the Regions Fund and $20bn Re-Wiring the Nation – will faster enable this pivot, allow banks to manage their risk return outcomes, plus act as a multiplier by crowding in additional private financing for key transition technologies.

We ended last year on a high note, with progress towards an internationally-aligned standard for climate-related financial disclosures and Treasury's consultation paper on key considerations for its design and implementation. The reporting framework will improve consistency and comparability of climate-related reporting in Australia, especially large firms and financial institutions where it counts. Treasurer, Jim Chalmers, acknowledges that this framework is essential to mobilising our financial system behind the net zero transition. We also start 2023 with the Safeguard Mechanism building credible momentum towards a formal carbon price for Australia and an Australian Carbon Border Adjustment Mechanism.

Complementing the move towards standardised climate disclosures is the Australian Sustainable Finance Institute's (ASFI) release of an initial set of recommendations for an Australian sustainable finance taxonomy, also open for public consultation. Sustainable taxonomies the world over have drawn much debate, with Canada's transition taxonomy paused earlier last year due to differences of opinion among committee members on fundamentals to the taxonomy. Europe's sustainable finance taxonomy also continues to stimulate debate around its Article 8 'light green' and Article 9 'dark green' provisions – funds have been fleeing light green constructs which 'promote' environmental and social benefits in favour of dark green funds which more actively and direct finance towards credible sustainable objectives.

With Australian Ethical last year reporting a 33% YoY increase in funds under management, the consumer is voting with their savings, and stakes have never been higher for Australia to regulate sustainable finance to attract and direct capital towards the transition. ASFI and Chalmers' co-ordinated approach to disclosures and a sustainable finance taxonomy will further accelerate climate financing momentum in Australia. This, combined with a promise to confront and crack down on greenwashing, is fostering greater credibility in the realm of sustainability-related targets, products and investments.

CBA provides 23% of all bank lending and plays a role in more than 40% of all financial transactions in Australia. They therefore can lead purposefully by lending to support the transition, helping customers navigate it, and leading the transition conversation.

Summary and highlights:

- CBA's **Green, Social and Sustainability Funding (GSSF) framework and its related Impact Report** sets an industry benchmark in sustainable finance transparency as we await finalisation and release of the ASFI taxonomy
- CBA achieved $30bn in new environmental lending in FY2021 and FY2022 combined, leaving $40bn to fund in 8 years under its $70bn climate pledge to FY2030. As Australia's largest bank, **we call for an increased ambition of $200bn to FY2030** and for CBA to accelerate the pivot of its balance sheet to financing Australian climate solutions
- **CBA leads the market on the financing of green residential buildings** having allocated $19.5bn in new and incremental lending to this asset class in the past two years
- Reductions in oil and gas exposures mean that CBA has successfully **met and exceeded its 2030 emissions reduction targets on oil and gas extraction under the NZBA**
- CBA is measuring and tracking **engagement with 82 of its highest emitting customers** and we look to evidence of how this translates to credible action
- **CBA has gotten the energy exposure trend right** – increasing exposures in renewable energy while decreasing exposures in coal, oil and gas over time

1. Climate solutions financing

Green, Social and Sustainability Funding Framework (GSSF)

The GSSF framework establishes the criteria underpinning CBA's green and social bonds, and sets a new benchmark in transparency within Australian sustainable finance among the banking majors as we await finalisation and release of the ASFI taxonomy.

Under this framework, 'use of proceeds' will be determined against CBA's definition of green and social eligible assets, with fossil fuels being among the excluded assets.

The framework also drives CBA's impact report which currently provides excellent detail against solar, wind, clean transport and green building projects as a result of green bonds issued by CBA.

Examples of performance measures for Green Eligible Assets

Renewable energy
- CO_2 emissions avoided (tCO_2e)
- Total installed capacity (MW)
- Reduction in particulate matter (tonnes).

Green buildings
- CO_2 emissions avoided (tCO_2e)
- Floor space of green real estate (m²)
- Location and type of certified Green Buildings
- Energy consumption (kWh/m² per year).

Energy efficiency
- The amount of lettable area (m²)
- The rate at which the property exceeded the benchmark
- CO_2 emissions avoided (tCO_2e)
- Energy efficient savings (MW).

Clean transportation
- CO_2 emissions avoided (tCO_2e)
- New clean infrastructure built (km)
- Number of passengers carried per annum.

Sustainable water and wastewater management
- Volume of water saved/reduced/treated (m³)
- Total population served by the system.

Pollution prevention and control
- CO_2 emissions avoided (tCO_2e)
- Waste diverted from landfill (tonnes).

Land use
- CO_2 emissions avoided (tCO_2e)
- Hectares of land rehabilitated
- Number of trees planted per km² of land.

Climate change adaptation
- Number of different climate change adaptation measures
- AUD expenditure on climate change adaptation measures.

Image 1: Example measures used to report management of proceeds on green assets

An external review by Sustainalytics provides an independent assessment of the GSSF framework's alignment with current market standards and the extent to which the eligible asset categories are credible and impactful. Overall, the framework is a great step by the bank to be transparent and align with global best practice and we would expect the framework to evolve to incorporate leading climate science, like the Chubb Review recommendations where appropriate.

Sustainability Funding Target

Scope – CBA's $70bn pledge over 10 years to FY2030 includes both environmental and social lending.[1] The $70bn is measured as 100% on balance sheet loans, not including the bank's facilitative role in crowding in capital through underwriting, advising or arranging deals.

Progress – CBA has achieved close to half its $70bn pledge in just two years (see Image 2 below), with 64% coming from green residential buildings.

Asset class ($bn)	30 June 2020 balance of lending	New and incremental financing since 1 July 2020
Green residential buildings	24.1	19.5
Sustainability-linked loans	0.7	4.8
Low carbon commercial buildings	4.5	3.2
Renewable energy	2.9	2.5
Social assets	0.2	0.4
Low carbon transport	1.0	0.2
Pollution/waste management	0.1	0.0
Energy efficiency	0.0	0.0
	33.5	**30.6**

Image 2: CBA's progress towards its Sustainability Funding Target

CBA reports the highest yearly environmental lending figure out of Australia's four major banks, at ~$15bn per year. Given CBA's market cap is, to take one example, 2.5 times ANZ's it could it also be argued that ANZ is performing relatively better in climate solution capital allocation. However, CEF notes that each bank measures new environmental lending in significantly different ways and it is, therefore, not a like-for-like comparison.[2]

Ambition – At the current rate, CBA will achieve $120bn on balance sheet capital allocation towards climate solutions between now and FY2030 (8 years), surpassing even ANZ's new benchmark pledge of $100bn within the same time period. As Australia's largest bank by market share and market capitalisation, we call for CBA to establish an even greater $200bn target by FY2030 which we see as absolutely achievable given key domestic policy shifts that

[1] CEF estimates environmental asset classes account for 99% of CBA financing activity to date. New and incremental lending against the sustainability funding target includes $0.4bn in social assets and $4.8bn in sustainability linked loans.
[2] This is an area that CEF plans to dive deeper into this year to determine additional factors impairing comparability across the sector. Formalisation of ASFI's Australian taxonomy will help.

start to align with the climate science and will stimulate the market for Australian climate solutions this decade. A greater public leadership commitment by CBA to pivot its balance sheet towards climate solutions will reinforce positive market signals and work to crowd-in capital to a growing Australian landscape of green projects.

Greening Australia's residential sector

What are green residential buildings?

Residential buildings are responsible for around 24% of overall electricity use and 12% of total carbon emissions in Australia. The important overhaul to the Nationwide House Energy Rating Scheme (NatHERS) late last year means that "greening residential buildings" across Australia now encompasses two dimensions. The first is the home's built design – construction materials for walls, insulation, double-glazed windows, roofs etc. The second is the home's energy performance – driven by installed solar capacity, battery storage (potentially from an EV on-site), and major appliances like hot water, heating and cooling etc. The NatHERS rating scheme, administered by the federal government on behalf of the states, is being used by the finance sector to underpin green loans and drive the greening of the residential sector. We also need better national climate risk mapping of both physical and transition risks (flooding, bushfires, sea level rise, heat stress, structural industry changes et al).

CBA progress and assessment

CBA and Westpac are the two banks with an outsized responsibility to lead the pivot finance toward greening residential buildings given they occupy 25% and 21% of the mortgage market share respectively – i.e. nearly half Australia's home loans market.

CBA reports a $24bn loanbook in green residential properties, which represents 4% of its total mortgage book valued at $620bn as at end FY2022. It also reports $19.5bn in new and incremental green home financing in the past two financial years combined. The bank acknowledges that greening the power grid, plus full electrification and improved thermal efficiency of homes, will assist in reducing household emissions and improve loan servicing capacity by reducing energy bills, both key outcomes.

Financing under this asset class includes new residential buildings which represent the top 15% of properties in the relevant jurisdiction in terms of local market carbon performance, and loans for properties with renewable energy output, governed in accordance with Climate Bonds Standards for Australia, Green Building Council of Australia, and/or NatHERS 5+ star rating. A limitation may exist with the NatHERS proxy where Sustainalytics notes that NatHERS 6 star ratings and above corresponds to the top 15% energy performing buildings in a few Australian jurisdictions, but there is insufficient data available to verify its use in all of Australia. We are encouraged by the preliminary efforts of CBA to map residential lending climate risks, given this is the single largest asset class in the Australian economy. We also need lending tools to drive investment in housing efficiency upgrades (e.g. compulsory NatHERS star rating certificates at the point of sale to drive adoption and valuation).

2. Financed emissions reduction by sector

Importantly, CBA joined the Net Zero Banking Alliance (NZBA) in January 2022, and set targets for three priority sectors – thermal coal, power generation, and oil and gas extraction[3]. By 2025, CBA intends to have sector targets established for 75% of financed emissions, based on a FY2020 baseline. We assume future sectors will include CBA's Australian home lending which accounts for 66% of CBA's drawn lending exposure and 15.5% of FY2020 financed emissions.

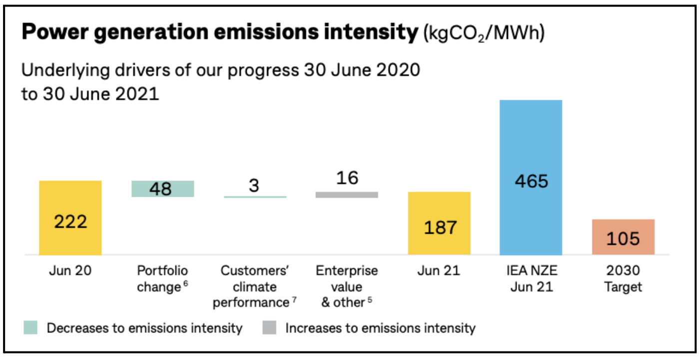

Image 3: Power generation portfolio, underlying drivers of progress

Thermal coal – like other Australian and global banks, CBA plans a 100% reduction in lending to thermal coal mining by FY2030.

Power generation – CBA commits to 53% emissions intensity reduction on a FY2020 baseline of 222kg CO_2-e/MWh, taking its FY2030 absolute target to 105 kgCO_2-e/MWh – lower than ANZ and NAB, and on par with Westpac.

Progress since FY2020 shows a 16% reduction in emissions intensity, equivalent to 35 kgCO2/MWh, primarily driven by portfolio changes – i.e. more renewables and less coal and gas (Image 3).

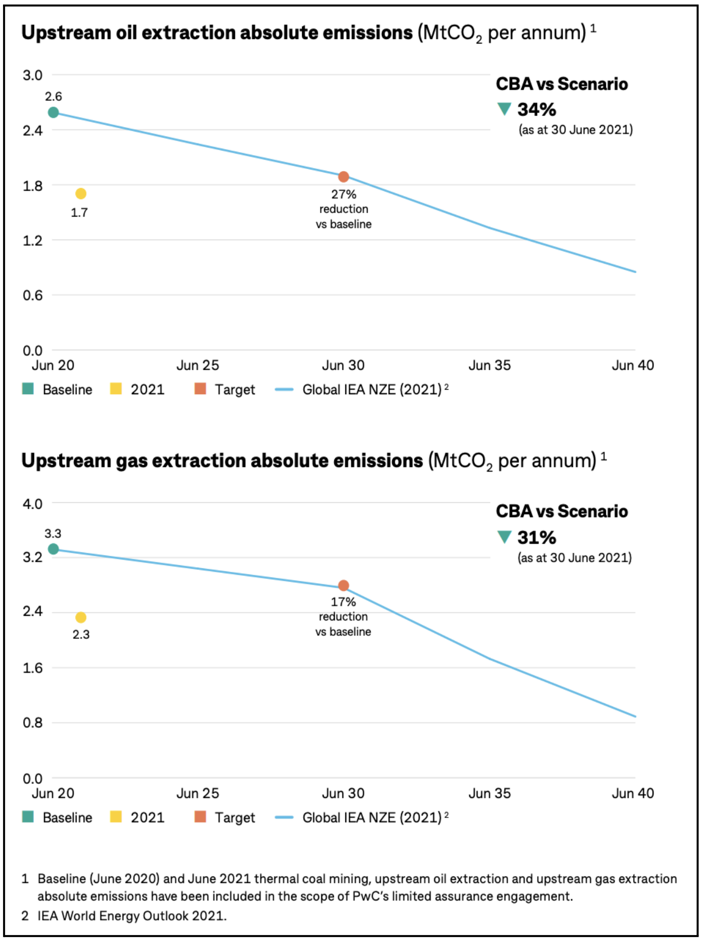

Image 4 – Oil and gas portfolio decarbonisation pathways

Oil and gas – CBA targets a 27% and 17% reduction on oil and gas portfolio emissions, respectively, based upon the global IEA NZE transition pathways for both sectors. As of FY2021, CBA has met and surpassed these targets (Image 4), with progress driven by reduced exposure to upstream oil extraction and upstream gas extraction by a combined 38%, from $2.9bn to $1.8bn between FY2020 and FY2021.

[3] CBA treats oil and gas targets individually which is different from NZBA and the other major Australian banks

Technically, CBA's oil and gas sector emissions portfolio could increase from today's levels if CBA maintains its alignment with the global IEA pathway, however, the bank acknowledges that analysts and investors have their eye keenly on this graph and would face criticism if its emissions profile were to increase by virtue of increased lending into the sector, as opposed to due to commodity price volatility.

3. Customer transition plan engagement

In FY2022, CBA reviewed 100 of its most carbon intensive customers and engaged with 82 to understand how they were assessing climate-related risks and opportunities (see climate report, page 22). They explored customers' transition readiness through:

- Interviews focused on climate-related governance, strategy, risk management, and metrics and targets
- Asking customers specifically about their transition plans, and complementing the effort with a quantitative analysis of a subset of these customers

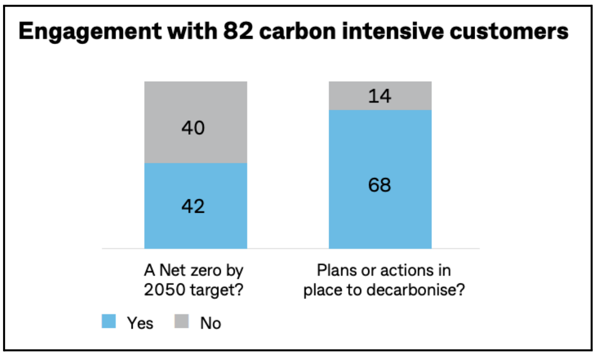

Image 5 – CBA's customer engagement

Results of 82 customers engaged:

- Half (42 customers) have a 'net zero by 2050' target
- 83% (68 customers) have plans or actions in place to decarbonise
- 22 customers reported having their own definition of a 'transition plan'.

CBA said the exercise highlighted opportunities to support customers, including accessing carbon markets; issuance of sustainability-linked loans; loan syndications; debt capital market activity; and structured asset finance opportunities.

4. Energy loanbook trends

CBA has, so far, gotten the trend right – increasing exposures in renewable energy while decreasing exposures in coal, oil and gas over time. CBA's combined exposure to coal, oil and gas[4] is $2.8bn, a 19% YoY decrease and a 40% decrease since FY2020. Renewables exposure, at $4.9bn,grew by 2% YoY and 17% since FY2020. CBA's renewables exposure is second to NAB's at $5.4bn.

It is great to see CBA disclose a significant amount of detail at the solar and wind project level in its Impact Report – making it possible to track how this expands in June 2023. CBA has also consistently disclosed its exposure across the energy value chain for a number of years, providing transparency and comparability in energy financing over time.

[4] Combined value of upstream thermal coal, oil, gas plus coal and gas electricity generation

CommBank reference list 2022

1. Annual report
2. Full year profit announcement
3. Climate report
4. Sustainability reporting appendix
5. Green, Social & Sustainability Funding Framework
6. Sustainalytics Second Party Opinion on Green, Social & Sustainability Funding Framework
7. Green, Social and Sustainability Funding – Impact report