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Mitsubishi UFJ Financial Group (TSE: 8306) (MUFG)
Sumitomo Mitsui Banking Corporation Group (TSE: 8316) (SMBC Group)
Mizuho Financial Group (TSE: 8411) (Mizuho) (collectively megabanks)

Failure to set targets, align portfolio exposure and policies with commitments leaves megabanks at serious financial risk

MUFG, SMBC Group and Mizuho' climate policies, targets and transition plans lack credibility, as they fail to align with a net zero emissions by 2050 pathway and global standard-setting initiatives such as the Net Zero Banking Alliance (NZBA) and the Task Force on Climate-Related Financial Disclosures (TCFD), despite repeated requests from investors. These failures have serious consequences: the megabanks are highly significant to the global and Japanese economy and have been identified by the Financial Stability Board in consultation with Basel Committee on Banking Supervision as global systemically important banks. With the IPCC's latest report demonstrating the drastic and urgent action needed to meet the Paris Agreement's 1.5 degree goal, the banks must disclose Paris-aligned transition plans to ensure they are adequately managing the immense climate-related financial risks they are exposed to.

Market Forces, Kiko Network and a representative of Rainforest Action Network (RAN) in Japan have filed shareholder proposals (full details on pp.11-12), requesting that the megabanks disclose plans to align their portfolios with a net zero by 2050 pathway. Investors are urged to request these disclosures through engagement with the megabanks.

At the upcoming megabanks AGMs, investors are urged to vote FOR the 'Transition Plan (Portfolio Alignment)' shareholder proposals (see pp.11-12).

Key Points

- **MUFG, SMBC Group and Mizuho's policies are not in line with their commitments,** including under the NZBA and to achieve net zero emissions by 2050. **The megabanks lack key and credible short and mid-term targets in emissions-intensive** sectors such as power, coal mining, and oil and gas, which are required to guide action and for investors to track progress.

- The megabanks appear to rely on “transition finance” and unproven technologies to reduce emissions, without providing sufficient disclosure for investors to be confident in the likely impact of these approaches.
- **The megabanks are falling behind their peers** involved in emerging markets, such as HSBC, DBS and others in target setting, with real world impacts in Indonesia, India and East Africa.
- Mizuho, MUFG and SMBC Group have indicated they are engaging with their clients in order to help them transition, but **without clear metrics and targets aligned with 1.5 degrees of warming, investors are unable to assess the effectiveness and progress of this engagement**.

Policies and targets incompatible with NZBA and net zero commitments

As described in the chart below, the megabanks’ current targets and policies have major shortcomings, failing to align with a globally recognized net zero scenario, or the standards set by the NZBA. As an example of the impact of these shortcomings, a recent study shows that **even after joining the NZBA, the megabanks ranked among largest financiers of companies expanding fossil fuels among NZBA banks globally** (MUFG: 3rd, Mizuho: 5th, SMBC Group: 9th).

The major gaps in the banks’ policies that allow such significant financing of fossil fuel expansion are:

- **Lack of portfolio-wide short- and mid-term targets -** none of the banks have set and disclosed lending and investment portfolio targets for 2030 or sooner targets, directly contradicting NZBA recommendations and similar TCFD guidance, which make it clear that “any medium- and long-term targets should have interim targets set at appropriate intervals (e.g., 5–10 years) covering the full medium or long-term target time horizon”.
- **Existing targets out of line with the global 1.5 degree goal, NZBA and IEA Net Zero** - the megabanks' existing targets (2030 financed emissions reduction targets for power and energy sectors) and relevant policies are not aligned with the Paris Agreement 1.5 degree goal, the NZBA requirements and the widely-referenced Net Zero by 2050 scenario (NZE) published by the International Energy Agency (IEA).

During our engagement with the banks, it has become clear that they are using governments’ policies and Nationally Determined Contributions (NDCs) that are not aligned with the 1.5 degree goal when assessing clients’ plans and projects for “alignment with the Paris Agreement”. The IPCC AR6 Synthesis Report has warned that current policies would lead to global warming of 3.2 degrees by the end of the century, and even strengthening policies to meet NDCs would see 2.8 degrees of warming.

The NZBA requirements represent the consensus of an industry-led, UN-convened group of banks, committed to aligning their lending and investment portfolios with net zero emissions by 2050. All the three megabanks have joined the alliance (MUFG in June 2021, SMBC Group and Mizuho in October 2021), and therefore are subject to these requirements.

The IEA NZE scenario is a conservative projection of the energy transition required, as it provides just a 50% chance of limiting global warming to 1.5°C and relies heavily on unproven low emissions fuels and negative emissions technology. However, it is one of the most widely used scenarios globally and is referred to in the NZBA guidance as one of the “credible, well-recognized” scenarios. The IPCC AR6 Synthesis Report includes 1.5 degree scenarios that cover sectors beyond energy.

Chart: Comparison of megabanks' policies and targets with IEA NZE and NZBA guidance

IEA NZE scenario	NZBA requirements	MUFG	SMBC	Mizuho
NZE scenario general energy sector decline:				
Emissions across the energy sector fall by a collective 39% from 2021-2030 in the NZE2050 scenario*	Targets shall include sector-specific and/or portfolio-wide targets for 2030 or sooner	No portfolio-wide target for 2030 or sooner		
	Lending shall be covered and on-balance sheet investment activities should be included	2030 Financed Emissions (FE) reduction target for power and energy sector only covers lending		
Oil and gas sector:				
"Beyond projects already committed as of 2021, there are no new oil and gas fields approved for development in our pathway."		No policy to rule out financing to **new and expansionary oil and gas projects or companies pursuing those projects** **		
"The rapid fall in LNG after 2030 in the NZE Scenario implies no need for additional capacity beyond what is existing or under construction (as of October 2022)		No policy to restrict financing to new LNG facilities		
Emissions from oil and gas fall by 29% from 2021-2030		2030 FE reduction target ranges from just 15% and is limited to upstream businesses, **excluding significant midstream and downstream emissions**	2030 FE reduction target ranges from just 12% and is limited to upstream businesses, **excluding significant midstream and downstream emissions**	2030 FE reduction target ranges from just 12% and is limited to upstream businesses, **excluding significant midstream and downstream emissions**
Coal mining sector:				
No new coal mines or mine lifetime extensions are approved from 2021	Clients with >5% revenues from thermal coal mining activities shall be included in the scope of targets	Policy allows for financing **expansion of existing projects, related infrastructure, companies expanding thermal coal mining and metallurgical coal mines**	Policy allows for finance of **companies expanding thermal coal mining and metallurgical coal mines**	Policy allows for finance of **companies expanding thermal coal mining and metallurgical coal mines**
Unabated coal supply falls by 48% from 2021-2030, and by 91% from 2021-2050		**No FE reduction target for 2030**	2030 FE reduction target ranges from 37%	**Zero FE for coal mining in OECD countries by 2030 and in non-OECD countries by 2040**
Power Sector:				
No new coal-fired power plants are approved from 2021	Clients with >5% revenues from electricity generation activities shall be included in the scope of targets	Policy allows for finance of **companies expanding coal power**		
Phase-out of unabated coal in advanced economies by 2035 and all unabated coal power plants by 2040.	Disclose well-recognised 1.5-degree scenario(s) (e.g., IEA, IPCC) with no- or low-overshoot, rely conservatively on negative emissions technologies	Coal power zero credit balance*** target by 2040	Coal power loan balance**** target by 2040	Coal power zero credit balance ***** target by 2040
		Unproven decarbonization technologies will be supported **without disclosure of financed emissions trajectories**		
Emissions from power and heat generation fall by 51% from 2021-2030.	Absolute emissions; and/or Sector-specific emissions intensity (e.g., CO2 e/ metric)	No absolute reduction target. Intensity targets do not guarantee absolute emissions reduction		
Agriculture sector:				
Absolute emissions; and/or Sector-specific emissions intensity (e.g., CO2 e/ metric)		No absolute reduction target No intensity target		

*The NZE is quite conservative on this point. According to the IPCC AR6 Synthesis Report: Climate Change 2023, in order to limit warming to 1.5°C (>50%) with no or limited overshoot, global greenhouse gas emissions will need to be reduced by 43% in 2030 compared to the 2019 level and CO2 emissions by 48%
**Mizuho's updated policy published on April 3 (in Japanese only as of April 5) will only require enhanced due diligence in financing new oil and gas extraction projects
***"Credit amounts related to coal-fired power generation project finance" and "corporate finance for coal-fired power generation" (MUFG Metrics and Targets)
****"Project finance and facility linked corporate finance (loan balance)" (SMBC TCFD Report 2022 and Strengthening Efforts against Climate Change)
*****"Credit balance for coal-fired power generation facilities" (Mizuho TCFD Report 2022)

Whilst the energy sector accounts for the overwhelming majority of global GHG emissions, the AFOLU (Agriculture, Forestry and Other Land Use) sector is the second largest source.

SMBC, Mizuho and MUFG have been among the fourth biggest lenders to large scale (more than 50MW) wood pellet biomass-fired power plants in Japan. They release more CO2 than coal plants at the point of combustion, per unit of energy generated.[1] Therefore, use of woody biomass as fuel in large-scale power generation is not viable as a climate solution (Chatham House, European Commission, Partnership for Policy Integrity, etc).

Overall, the megabanks' policies, targets and practices are inconsistent with 1.5-degree pathways, contradicting the banks' own commitments to the NZBA and to achieve portfolio-wide net-zero by 2050.

Lack of transparent and effective engagement on clients' transition plans

Financial institutions are able to leverage their position as a source of capital to influence changes in the economy urgently needed to address the climate crisis. None of the Japanese banks have sufficiently disclosed how they would manage and support the transition of their clients, despite client engagement appearing to be the basis of the banks' portfolio emission reduction strategy.

The banks' current engagement policies lack clear expectations with specific measures for their clients' transition plans, such as timelines, pathways, metrics, and targets. Therefore, it is unclear how banks even evaluate – let alone ensure – clients' alignment with climate goals.

In addition, the megabanks' engagement policies lack escalation plans. There are no explicit conditions for withdrawing financial support from clients that are lagging behind the transition. These lack of processes are out of line with recommendations – including by SBTi and the High-Level Expert Group on Net Zero – that financial institutions have escalation policies to enhance engagement activities. Investor groups such as TPI, and IIGCC have recommended banks to have explicit criteria for financing to misaligned clients.

[1] GHG protocol and SBTi's Net Zero standard require that companies shall report biogenic CO_2 emissions including combustion of biomass. IPCC also mentions 'When using inventory estimates to assess the CO_2 emissions arising from energy use, including wood for energy purposes, it is necessary to consider relevant emissions estimated in the Energy and AFOLU sectors.' National Greenhouse Gas Inventory Report of Japan shows that carbon emission factors for fuel combustion in gross calorific value for coal power generation use is 24.3(t-C/TJ) and woods (biomass) is 29.6(t-C/TJ).

The following case studies demonstrate the real-world impact of the gaps in the megabanks' policies:

Adaro Energy Indonesia (Coal)

In April 2021, SMBC participated in a US$400 million loan to Adaro Energy Indonesia, a coal giant with more than 90% revenue from coal mining. Adaro's subsidiary is planning to build a new coal power plant for its aluminium smelter in North Kalimantan, Indonesia.

The scale of new coal power capacity required is staggering. The smelter intends to produce 1.5 million tonnes per annum at full capacity, at least two-thirds of which would be powered by coal. It would require at least several gigawatts of new coal-fired power plant capacity to make this possible. The smelter's existence depends on building massive new coal-fired power capacity, meaning without a policy to restrict corporate finance that can be used for a new coal power plant, the megabanks can finance the Adaro group and enable new coal power at a gargantuan scale.

A woman as she waits to be evacuated in front of her flooded house in South Kalimantan, Indonesia. The flooding has been linked to massive land clearing for coal mining activities, including Adaro, in South Kalimantan. © Putra / Greenpeace.

Adani Enterprises (Coal)

Mizuho FG, MUFG and SMBC Group are all bond arrangers for Adani Enterprises, the parent Adani group company responsible for the disastrous Carmichael thermal coal project in Australia. The Adani group, specifically Adani Enterprises, is also now the largest private developer of new coal mines and coal power plants in the world. In addition to its massive coal expansion plans, the recent allegations leveled at the Adani group by Hindenburg Research have caused a massive drop in the share price for the whole group with several investors divesting their shares, such as Norges. Despite the allegations, all three banks were named in arranging a fixed-income roadshow for the group as recently as late February 2023, as they have no explicit restrictions around underwriting corporate bonds for companies expanding coal power or mining. Given the massive fossil fuel expansion plans of the Adani group and the Hindenburg allegations, it is unclear how Mizuho, MUFG and SMBC could be seen as taking climate and ESG concerns seriously while still arranging bonds for the Adani group.

(Credit: Stop Adani)

Without sufficient restriction on corporate financing and clear expectation for client's transition strategy, the banks can still finance companies pursuing new coal mines and coal power plants like Adani and Adaro.

East African Crude Oil Pipeline (Oil and Gas)

One of the most controversial fossil fuel expansion projects in Africa is the US$5 billion, 1443-kilometer East African Crude Oil Pipeline (EACOP), which would transport 216,000 barrels per day of electrically heated crude oil extracted from the Tilenga and Kingfisher oilfields in Uganda to the port of Tanga in Tanzania for export.

SMBC is acting as financial advisor to French oil major TotalEnergies (Total) – the lead developer of the project – and joint lead arranger for the $3 billion project loan that will provide the majority of the financing for the project. [50 global financial institutions and export credit agencies] have publicly ruled out involvement in EACOP already, owing to its unacceptable environmental, social and governance (ESG) risks. Mizuho has also ruled out financing EACOP as long as the ongoing E&S issues are not resolved. MUFG has remained silent on its financing plans. None of the megabanks have policies and targets relating to mid-stream oil and gas.

(Credit: Stop EACOP)

Disclosure on financed emissions trajectories required given reliance on unproven technologies

As noted above, none of the three megabanks have provided sufficient disclosure of their financed emissions trajectories to achieve net zero by 2050, which renders investors unable to assess credibility of banks' plans and strategies. It is especially concerning as there is no clarity on how much banks would rely on unproven technologies such as ammonia/hydrogen co-firing and CCUS (carbon capture, utilisation and storage) in attempting to achieve their net zero goals.

All three megabanks are actively involved in new technology development by funding the Green Transformation (GX), particularly MUFG and Mizuho. This fund includes the utilization of fuel ammonia/hydrogen and CCUS. MUFG's proactive stance on GX is reflected in the formulation of the White Paper on Transitions, the first of its kind for a Japanese bank and development of guidelines for "transition finance" to facilities and projects in Southeast Asia and elsewhere to decarbonization. Mizuho also increased[2] the scope of its transition finance to include investments in "highly uncertain seed" and "early-stage technology" development.

The megabanks' policies allow them to support unreliable co-firing and CCUS technologies, which can prolong coal power use, in the name of "transition to decarbonization" despite their restrictions on new and expansionary coal power projects. There is little evidence suggesting the commercial viability of these technologies to meet a net zero by 2050 outcome or about their lifecycle emission reduction capabilities. Many studies have pointed out these unproven technologies are not only financially risky but also questionable in reducing emissions and would potentially lock-in ongoing usage of fossil fuels (Transition Zero, Energy Transitions Commission, ISS, BNEF, IEEFA etc).

NZBA's guidance states scenarios used "shall be no or low overshoot" and "shall rely conservatively on negative emissions technologies". The megabanks must therefore disclose their reliance on these technologies in their financed emissions trajectories.

MUFG, SMBC Group, and Mizuho lagging behind peers

Peer financial institutions are placing more effective restrictions on finance to companies and projects expanding fossil fuels, leaving MUFG, SMBC Group and Mizuho with clearly ineffective policies and targets behind.

Examples of progressive policies and disclosure of targets by peer financial institutions

Oil and Gas	**HSBC** December 2022	No longer provide new finance (through lending or capital markets) for the specific purpose of projects pertaining to new oil and gas fields and related infrastructure when the primary use is in conjunction with new fields.
	DBS 2022	DBS's "absolute emissions targets for the O&G sector cover upstream, downstream and integrated companies".
	ING March 2022 & March 2023	Restrict dedicated finance (lending or capital markets) for upstream oil and gas fields (exploration and extraction) approved for development after 31 December 2021, and for midstream (oil and gas infrastructure) activities.
	Danske Bank March 2021	Committed to immediately end direct finance for the expansion of oil and gas exploration and production worldwide.

[2] Available only in Japanese as of April 10.

	La Banque Postale October 2021	Committed to immediately “refraining from financing oil and gas energy projects”, “no longer providing financial services” to upstream and midstream oil and gas companies, and “a complete withdrawal from fossil fuels by 2030”.
	Nordea Asset Management February 2023	“Nordea does not provide project financing dedicated to expanding exploration of new oil and gas fields.”
Coal	CIMB December 2020	“Prohibits asset-level or general corporate financing for new thermal coal mines and coal-fired power plants, as well as expansions, except where there is an existing commitment.”
	HSBC December 2022	Will not provide new finance to any client, or new advisory services in connection with specific purposes such as new captive thermal coal-fired power plants or new captive thermal coal mines and new metallurgical coal mines. Will not start a relationship with a new company in the mining sector with annual thermal coal revenues are ≥10%, or thermal coal production is >5Mt, or thermal coal, as a by-product from the extraction of metallurgical coal, is >15% of total production volumes. Same for coal power clients with operational thermal coal power generating capacity is either ≥10% of total generating capacity or ≥1GW.
	Nordea Asset Management February 2023	“Nordea does not initiate any new financing relationships with companies having more than 5% of their revenues coming directly from thermal coal, covering coal-fired energy production companies and/or mining companies that are extracting thermal coal. We do not finance or refinance companies with expansion plans for thermal coal or new and pre-construction phase thermal coal activities.” “Nordea does not invest in companies with substantial and sustained exposure to coal mining, defined as having a 5% revenue threshold on thermal coal and 30% revenue threshold on total coal (including metallurgical coal). By 2025, Nordea will phase out investment in coal-related companies without plans to achieve a full exit from coal globally by 2040.”
Engagement	HSBC December 2022	“If a transition plan is not produced or if, after repeated engagement, is not consistent with our targets and commitments, we won’t provide new finance, and may withdraw existing financing if appropriate.”

Investor action required

In the face of accelerating policy, market and investor commitments towards achieving net zero emissions by 2050, the 'Transition Plan (Portfolio Alignment)' shareholder proposals seek disclosure of credible measures and targets to align the banks' activities with this outcome. The co-filers have engaged with MUFG, SMBC Group and Mizuho on multiple occasions over several years on climate related strategies and actions, particularly regarding the management and disclosure of their climate-related risks. The co-filers have also conducted intensive engagement with the banks for the last a few months prior to filing the shareholder proposals.

While the banks have shown a willingness to engage on these issues, the engagement has not sufficiently raised hopes that the banks are committed to formulating and disclosing transition plans, including short- and medium-term targets, with credible, well-recognized pathways or trajectories to net zero emissions by 2050 or sooner, including strategic policy commitments and targets for significant GHG-intensive sectors within their portfolios, considering the full range of Scope 3 value chain emissions.

Investors should be wary that the megabanks' policies and practices are still far from aligned with the Paris Agreement 1.5 degree goal and fall well behind many global peers. Unless there is a significant strengthening of transition planning, MUFG's, SMBC Group's, and Mizuho's climate-related financial risk will remain extremely high and inadequately managed.

At the upcoming megabanks AGMs, investors are urged to vote <u>FOR</u> the 'Transition Plan (Portfolio Alignment)' shareholder proposals.

Shareholder Proposal Text

Partial amendment to the Articles of Incorporation (issuing and disclosing a transition plan to align lending and investment portfolios with the Paris Agreement's 1.5 degree goal requiring net zero emissions by 2050)

The following clause shall be added to the Articles of Incorporation:
Chapter X: "Transition Plan (Portfolio Alignment)"
Clause Y: "Issuing and disclosing a transition plan to align lending and investment portfolios with the Paris Agreement's 1.5 degree goal requiring net zero emissions by 2050"

1. In order to fulfil the Company's commitment to net zero emissions by 2050 in its lending and investment portfolios, the Company shall set and disclose a transition plan to align its portfolios, in the short-, medium- and long-term, with credible pathways to net zero emissions by 2050 or sooner, including strategic policy commitments and targets for significant GHG-intensive sectors within its portfolios, considering the full range of Scope 3 value chain emissions.
2. The Company shall report on its progress against such a transition plan and targets in its annual reporting.

Reasons for proposal

This proposal requests that the Company disclose information required for shareholders to determine the integrity of the Company's plans to achieve its net zero emissions by 2050 commitment, and for the Company to appropriately manage climate change risks, and maintain and increase the Company's long-term corporate value.

The Company is exposed to substantial financial risk, given its significant involvement in carbon-intensive sectors such as fossil fuels. However, the Company has not set and disclosed sufficient targets or policy commitments to align its exposures to the most GHG-intensive sectors with a net zero emissions by 2050 pathway.

It is, therefore, critical for the Company to ensure the integrity of its climate goals and transition plans by setting and disclosing such targets and strategic policy commitments, which should align with the trajectories and key conclusions of credible net zero emissions by 2050 scenarios, such as the International Energy Agency's. Global peers of the Company are already disclosing this type of information.

The disclosure this proposal seeks is commonly expected among investors through the Task Force on Climate-related Financial Disclosures (TCFD), and international standard setting initiatives such as the Net Zero Banking Alliance.

Shareholder resolutions in Japan and Amendments to Company Articles of Incorporation

- The proposal to amend the company's articles of incorporation in part is the most commonly used approach to make shareholder proposals in Japan, and the approach taken in this proposal. Around two-thirds of the shareholder proposals filed in 2021 took this form.
- Under Japanese corporate law, the sole legal pathway for a **shareholder proposal on climate change** is via an amendment to a company's articles of incorporation.
- The legal effect of such shareholder proposals is the same as the "special resolutions" on climate change filed and passed at UK companies including Barclays, BP, Royal Dutch Shell, Rio Tinto and Anglo American, which take binding effect as part of the companies' constitutions.

-- Client Earth

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