

# China's long and winding road to net zero

China is thought to account for over a quarter of global greenhouse gas emissions, and Paris Agreement alignment will be vital if global heating is to be kept within safe planetary boundaries. Haonan Wu examines the challenge.

## Setting the scene

China's economic and social development follows the Five Year Plan (FYP) model, developed by the central government. This approach was introduced in the 1950s and covers China's economic ambitions and societal goals for the next five years. The current FYP outlines an aim to become a "moderately developed" economy, while enhancing environmental protection and the green economy.

It focuses on domestic structural reforms to expand China's internal economy, limiting China's reliance on foreign countries, but sees China continuing to develop its Belt and Road Initiative. This is a colossal infrastructure project to build trade links and grow economies, similar to the historic Silk Road. The plan also sets targets for innovation and the improvement of the wellbeing and health of China's population through social investments.

## For further information please contact:



**Haonan Wu**  
**Sectors: Transportation,  
 Chemicals, Technology, Utilities**  
[haonan.wu@hermes-investment.com](mailto:haonan.wu@hermes-investment.com)

In the run up to the UN's COP26 climate talks, China's President Xi Jinping pledged that China would stop building new coal-fired power projects abroad – a significant commitment as China has been one of the biggest public financiers of new coal plants both overseas, and at home.<sup>1</sup>

China is the world's second largest economy, and is thought to be the largest greenhouse gas emitter. The Rhodium Group estimates that China was responsible for 27% of global greenhouse gas emissions in 2019<sup>2</sup>, with coal-fired power generation still accounting for around 50% of its energy mix.

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of global greenhouse gas emissions in **2019**, according to Rhodium Group estimates.

China has only committed to achieving carbon neutrality by 2060, rather than 2050, while aiming for carbon emissions to peak before 2030.<sup>3</sup> However, at the UN General Assembly in 2020, President Xi emphasised China's commitment to the Paris Agreement and low carbon development, increasing its nationally determined contributions (NDC)<sup>4</sup> to target a carbon intensity reduction of at least 65% by 2030.

<sup>1</sup> President Xi declares end to Chinese support for new coal power abroad ([climatechangenews.com](https://www.climatechangenews.com))

<sup>2</sup> China's Greenhouse Gas Emissions Exceeded the Developed World for the First Time in 2019 | Rhodium Group ([rhg.com](https://rhg.com))

<sup>3</sup> <https://eciu.net/netzerotracker>

<sup>4</sup> [https://www.fmprc.gov.cn/mfa\\_eng/zxxx\\_662805/t1817098.shtml](https://www.fmprc.gov.cn/mfa_eng/zxxx_662805/t1817098.shtml)

The fourteenth FYP, released in March 2021, updated China's climate target for the next five years, aiming to boost China's share of non-fossil fuel sources in its energy mix. With the inclusion of nuclear and hydropower, this is expected to increase to around 20% by the end of 2025, and there is a separate commitment to install 1,200GW of wind and solar capacity by 2030. Following the first joint announcement by the US and China on addressing climate change in 2014, a renewed statement in 2021 committed them to "work together and with other parties to strengthen implementation of the Paris Agreement". This is welcome momentum.

## Keeping the coal fires burning

However, the latest FYP contained references to the development of coal with an emphasis on "clean and efficient utilisation" for energy security and self-sufficiency purposes. China is still building more than 800 coal-fired power plants according to the Global Coal Exit List developed by Urgewald<sup>5</sup>, a database that identifies which companies are still developing new coal assets. The International Energy Agency's latest report setting out a roadmap to Net Zero by 2050<sup>6</sup> indicates that to achieve this goal globally, the development of any new coal plants must be halted from 2021. In another worrying sign, China's latest FYP lacked a clear coal consumption cap, a feature that had been included in the thirteenth FYP.

As the cost of renewable energy continues to decline and China's utilisation rates of coal-fired power plants fall, the existing coal asset base will become less economic to operate. Some estimates suggest that the Levelised Cost of Electricity (LCOE) for renewable energy and batteries is already comparable to the cost of operating coal-fired power plants in China. A report<sup>7</sup> from the Tsinghua University's Institute of Climate Change and Sustainable Development on China's low carbon development strategy also indicates that China needs to generate 90% of its electricity from non-fossil fuels and less than 5% from coal to achieve net-zero emissions under a 1.5-degree scenario by 2050.

According to its statements and the FYP, China is committed to tackling climate change and developing its economy in alignment with the Paris Agreement. However, the FYP falls short of a commitment to realistically limit global warming to 1.5°C by 2050 and is focused mostly on carbon emissions reduction, with only occasional mention of other key greenhouse gases such as methane.

It is certainly ambitious for China to achieve net zero by 2050 but it is not an impossible task, given its track record of rapid installation of solar and wind capacity in recent years. To actually deliver on its commitment to the Paris Agreement, China's power and heavy industry sectors must adopt a decarbonisation strategy immediately and limit the use of coal.



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We hope that sector-specific energy plans due to be published later this year will include detailed descriptions of decarbonisation pathways.

## Our engagement approach

In 2021 China's Securities Regulatory Commission (CSRC) released new guidelines recognising the importance of ESG issues and related disclosures. In their annual reports, companies must now disclose their environmental impacts, and the inclusion of any reductions in carbon emissions is encouraged. With China focusing on rural revitalisation to lift the population out of poverty, the FYP mentions improving the country's employment policy and healthcare system, alongside a focus on reforestation and modernising the agricultural sector.

We are engaging with Chinese and Hong Kong companies on establishing targets and plans for reducing greenhouse gas emissions in line with the Paris Agreement. For example, we have engaged with Geely Automobile, encouraging it to align its reporting and underlying processes with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). Geely took our suggestions on board and referenced the four pillars of the TCFD in its 2019 sustainability report, published in April 2020.

Another example is electricity company Power Assets, which we encouraged to improve its disclosure of carbon emissions and climate change management. Following our engagement, Power Assets disclosed group-level Scopes 1 and 2 emissions and environmental key performance indicators. It also integrated climate change with risk management.

As part of the collaborative initiative Climate Action 100+, we co-lead engagement with the Chinese oil and gas companies PetroChina, CNOOC and Sinopec, to ensure that net-zero commitments and decarbonisation strategies are aligned with the Paris Agreement. We are also part of the Asia Investor Group on Climate Change (AIGCC) and participate in its Asian Utilities Engagement Program (see box).

<sup>5</sup> <https://coalexit.org/>

<sup>6</sup> <https://www.iea.org/news/pathway-to-critical-and-formidable-goal-of-net-zero-emissions-by-2050-is-narrow-but-brings-huge-benefits>

<sup>7</sup> [https://mp.weixin.qq.com/s/S\\_8ajdq963YL7X3sRJSWGg](https://mp.weixin.qq.com/s/S_8ajdq963YL7X3sRJSWGg)

## AIGCC Asian Utilities Engagement Program launched



**The Asia Investor Group on Climate Change (AIGCC), of which we are a member, has launched a new programme to engage Asia's systemically important electric utilities on cutting emissions, strengthening disclosure and improving governance of climate-related risks.**

The AIGCC aims to create awareness and encourage action among Asia's asset owners and financial institutions about the risks and opportunities associated with climate change and low carbon investing. Its Asian Utilities Engagement Program was formed in June with 13 investors and stewardship service providers, including EOS, to increase the effectiveness of climate engagement with five companies. These are China Resources Power Holdings, Hong Kong's CLP Holdings, Japan's Chubu Electric Power Company and Electric Power Development Company (J-Power), and Malaysia's Tenaga Nasional Berhad.

These companies were selected because they produce substantial greenhouse gas emissions, have large coal-fired power capacity, or have a strategic role to play in driving the net-zero emissions transition. Together, these companies emitted approximately 285 million tonnes of CO<sub>2</sub> in 2019, equivalent to the national emissions of a country like Spain. Another issue is that Asian coal-fired power plants have an average age of just 13 years, but the average economic lifespan can be 40 years.

EOS is leading the engagement with Chubu Electric Power and is a collaborator on the J-Power engagement. We will seek greenhouse gas emissions reductions from these companies in a way that is aligned with the Paris Agreement. For example, we will ask them to set clear decarbonisation strategies with short-, medium- and long-term action plans including a timetable to phase out coal-based emissions in line with 1.5°C temperature scenarios.

Other focus areas for discussion in the initiative's shared agenda include asking for a strong governance framework that clearly articulates a board's accountability and oversight of climate change risks and opportunities, and enhanced corporate disclosure in line with the recommendations of the Task Force on Climate-related Financial Disclosures.

The initiative is intended to complement and run in parallel with Climate Action 100+ (CA100+), so Asian electric utility companies that are currently the focus of CA100+ were excluded from consideration.

**As part of our engagements with global steel manufacturers and mining companies, we have asked them to reduce carbon emissions along their value chains.**

We have included a climate change voting policy in our Corporate Governance Principles for Mainland China and Hong Kong, and we communicate our expectations with companies identified as climate change mitigation laggards.

Recognising the contribution that coal-fired power plants make to global heating, we have joined the Powering Past Coal Alliance (PPCA), a coalition working to advance the transition from unabated coal power generation to clean energy. This year we intensified our focus, writing to companies identified by the Global Coal Exit List, warning that if we were not able to gain sufficient information to understand the company's approach to climate change risk management, we would recommend a vote against the re-election of appropriate board members in line with our voting policy on coal.

As part of our engagements with global steel manufacturers and mining companies, we have asked them to reduce carbon emissions along their value chains. Miner BHP has agreed a five-year partnership with China Baowu with the intention of investing up to \$35m and sharing technical knowledge to help the steel industry decarbonise. BHP has also committed to reducing its Scopes 1 and 2 emissions by at least 30% by 2030 relative to 2020. The target is science-based and aligned with the company's ambition to be carbon neutral by 2050. We are increasing our focus in China to reduce coal supply chain emissions, including Scope 3 emissions.

### The road ahead

China's rapid economic development has come at the cost of the environment over the last two decades. However, in the "Two Mountains" theory often quoted by President Xi, clear waters and green mountains are seen as invaluable assets, and long-term growth should be twinned with environmental protection.

The FYP makes this clear by dedicating a whole chapter to green development and accelerating the low carbon transition. We will continue to engage with Chinese companies and policymakers to ensure this commitment is realised, encouraging a faster phase-out of coal and a reduction of carbon emissions so that global heating is kept within safe parameters.



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## Why EOS?

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## Contact information

**EOS**

**Dr Hans-Christoph Hirt** Hans-Christoph.Hirt@hermes-investment.com

For more information, visit [www.hermes-investment.com](http://www.hermes-investment.com) or connect with us on social media:



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