

Green Bonds – a key tool for financial centre competitiveness: Lessons from Europe

Financial centres have a vital role in scaling up sustainable finance action, as the places where demand for and supply of finance meet. In their different roles, financial centres can support the mainstreaming of sustainability risks and transform opportunities into market practices, across banking, capital markets, investing, insurance, and professional services.

This briefing gathers the experience of European financial centres with green bonds, and provides insights on how green bonds can be leveraged as a core pillar of sustainable financial centres.

It has been developed by the Climate Bonds Initiative as part of the Financial Centres for Sustainability (FC4S) Europe project, with the support of Climate-KIC.

Introduction

Financial centres are cities with an intense concentration of financial activity and often where financial regulation and public debate on financial performance develops.¹ Since COP21 in Paris, several major financial centres have launched green or sustainable finance initiatives reflecting a growing momentum towards sustainable finance, responding to policy, market and economic needs.

By harnessing the power of place, where demand and supply meet, financial centres have the potential to scale up green and sustainable financial services across capital markets, banking, fintech, insurance and investment.²

Capital markets are where some of the most prominent developments in sustainable finance have occurred in recent years – including the emergence and rapid growth of “green bonds” – bonds with proceeds dedicated to investments with environmental benefits, from climate change mitigation and adaptation, to air and water quality, biodiversity or coastal conservation. Through the green label, investments in assets aligned with a low-carbon and climate-resilient future have been made visible. In parallel, underlying definitions and standards for green bonds have evolved, breaking new ground for the development of other types of green finance instruments. Considered as a case study of sustainable finance market development, the growth story

Financial Centres for Sustainability (FC4S) Europe

FC4S Europe is the regional node of the UN Environment FC4S global network, launched in September 2017. The FC4S Network is a platform for financial centres authorities to exchange experiences and develop practical collaborations to build robust and liquid green and sustainable financial markets. FC4S Europe works to support pan-European green and sustainable finance efforts, including the EU Commission Action Plan for Financing Sustainable Growth.

of green bonds highlights the necessity to involve new market participants and actors, such as sustainability experts, civil society organisations, and individual consumers.³

Financial Centres & Green Bonds

Developing a domestic green bond market can support financial centres on their journey towards becoming fully sustainable, as it can help to:

- **Raise awareness around green investments:** green bonds have given proof to financial sector participants – investors, issuers, underwriting banks and rating agencies – that green and sustainable finance is an area of growth and opportunity.
- **Create a tool to facilitate investor-issuer engagement:** issuers report that green bonds have broadened their investor base and deepened their engagement levels with investors in the fixed income space, as they enquire about both the issuance and the company’s sustainability plans.
- **Develop a common understanding of what constitutes green investments:** As it is common practice for green bond issuers to disclose the use of proceeds to investors, definitions and standards are being developed in many jurisdictions to help harmonise the eligibility criteria of assets that are climate-aligned. The European Commission has proposed the establishment of regulatory frameworks to facilitate sustainable investment and has constituted a Technical Expert Group to advise on how such frameworks could be developed.⁴ Clear guidelines can also support foreign issuers that wish to raise green bonds overseas.
- **Support public policy for sustainable finance:** green bonds provide a tool to re-orient capital flows from brown to green through the existing market infrastructure. The public sector has played a catalytic role in the

green bond market and green bonds have contributed to moving the conversation on green finance into mainstream economic and financial sector deliberations including the G20 Green Finance Study Group, the Financial Stability Board’s TCFD process and the Network for Greening the Financial System.

Financial centre authorities, with their varying market development functions, can foster the development of green bond markets by:⁵

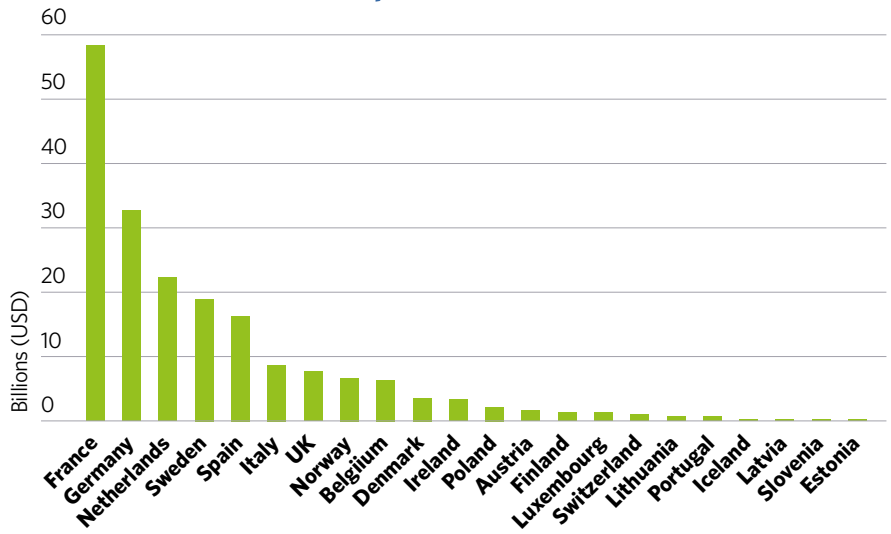
- **Supporting the development of guidance for green financial instruments:** Depending on the institutional structure of financial centre authorities, these can be in the form of regulation, guidelines or listing requirements
- **Developing new market infrastructure:** Financial centre authorities can work with key platforms to encourage the development of specific segments, indices, or other platforms. Several stock exchanges in Europe have created green bond segments, with minimum requirements around disclosure to drive standardisation. At the EU level, regulation on low carbon benchmarks, including Paris- aligned benchmarks, is currently being discussed.⁶
- **Implementing best practice on disclosure around sustainable investments and exposure to climate risks:** Financial centre authorities can engage with regulators and supervisors to encourage action to strengthen market discipline relating to green finance – including by requiring companies, investors and financial institutions to disclose exposure to sustainable investments and climate risks.⁷ The transparency and market practices around green bonds disclosure can help build reporting requirements around sustainable investments.

The Green Bond Market in Europe

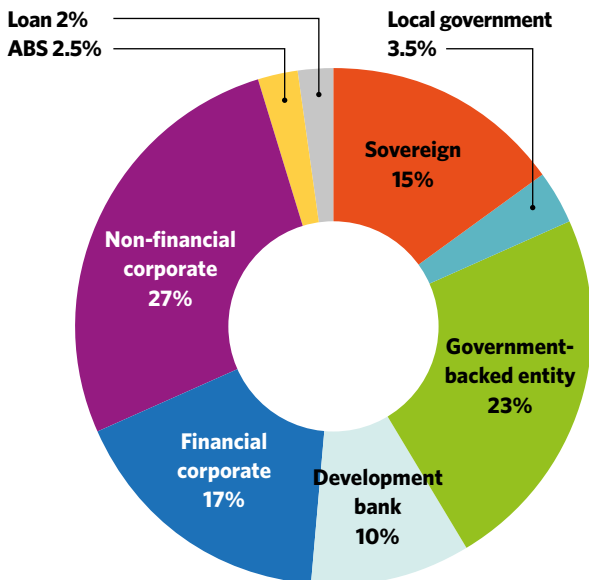
Globally, green bond markets have been exponentially growing since 2012 - with approximately USD500bn issued to date. Annual issuance of listed green bonds reached USD167.3bn in 2018, with the target for 2019 set at USD300bn. As a region, Europe hosts the largest green bonds market, with USD184.2bn worth of green bonds issued (see chart).

Europe has also pioneered several green bond market segments: the first ever green bond was issued in 2007 by the European Investment Bank and labelled as *Climate Awareness Bond*; in 2012, the Île-de-France region issued the first municipal green bond; in 2013 the Swedish property company Vasakronan issued the first corporate green bond; and in 2016 Poland issued the first green sovereign.

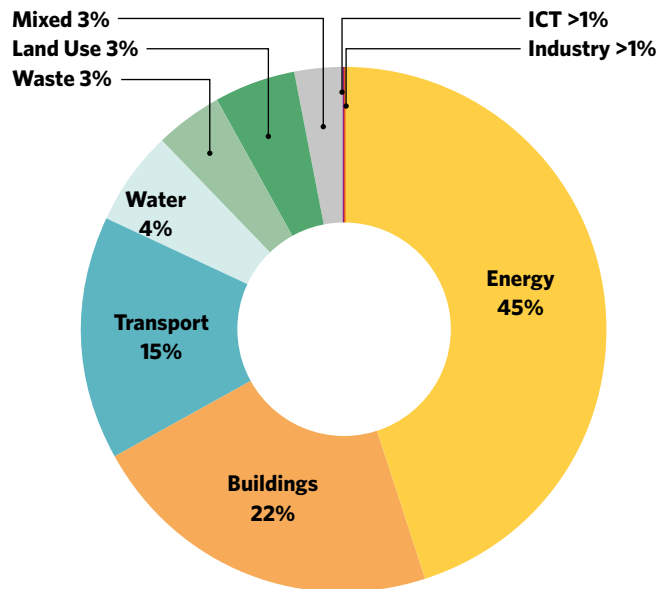
Green bond issuance in Europe



Europe - green bond issuance by issuer type



Europe - Use of Proceeds 2018



Key highlights of sustainable finance policy developments in Europe

Article 173 (Jan 2015): France becomes the first country to pass a law introducing mandatory extensive climate change-related reporting for asset owners and asset managers. Article 173 requires institutional investors to report on the integration of both physical risks and 'transition' risks caused by climate change on their activities and assets.

HLEG on Sustainable Finance (Dec 2016): The European Commission establishes a High-Level Expert Group (HLEG) on Sustainable Finance to provide advice on how to steer the flow of public and private capital towards sustainable investments, identify the steps that the financial institutions should take to protect the stability of the financial system from risks related to the environment and deploy these policies on a Pan-European scale. The HLEG releases two comprehensive reports in July 2017 and January 2018.

Swedish Inquiry (Dec 2016): The Swedish Government appoints an inquiry to promote the market for green bonds which recommended a sovereign green bond issuance.

UK Green Finance Taskforce (Sep 2017): The UK Government establishes a Green Finance Taskforce to accelerate the growth of green finance and deliver the investment required to meet the UK's carbon reduction targets. Following the Taskforce's final report in March 2018, the British government commits to establishing a Green Finance Institute, together with the City of London.

EC Action Plan on Sustainable Finance (Mar 2018): The European Commission (EC) releases its Action Plan on Financing Sustainable Growth with three subsequent legislative proposals on 1) establishing an EU classification system for sustainable activities; 2) incorporating sustainability in investor duties; 3) creating low-carbon benchmarks.

The Financial Centre Green Bond Ecosystem

Issuers: financial institutions, corporations, central and local governments, government-backed entities

Investors: pension funds, insurance companies, financial institutions (commercial and central banks), retail investors; these include general bond investors or dedicated green ones

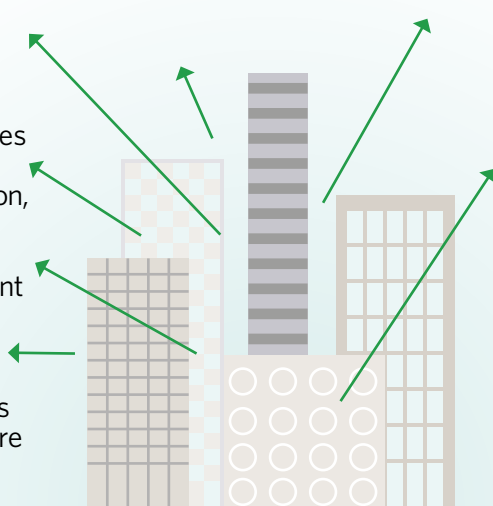
Stock exchanges: In Europe, London, Milan, Stockholm, Luxembourg, Frankfurt and Oslo have a dedicated green bond list/segment

Civil society: Environmental and climate finance NGOs can influence market players towards creating a more sustainable future

Verifiers: An independent review of green credentials of the bond is common practice in the European market. Verifiers include firms and consultants with accounting and environmental expertise

Policymakers: The European Commission has published a 10-point Action Plan on Sustainable finance which includes a taxonomy for sustainable activities, an EU Green Bond Standard and disclosure rules around sustainable investing

Regulators: Regulation for green bonds can be developed to clarify definitions; disclosure and climate-related risk management can also be promoted by regulators; monetary policy including prudential and collateral frameworks can also be designed to support low-carbon investments



Green bonds as a tool to develop green financial centres in Europe

Sharing experiences around green finance instruments, bringing clarity and convergence on definitions, taxonomies and classification systems, and building skills and capacity through peer exchange have been identified as strategic action points for the FC4S Network. The following section aims to gather the experience of European financial centres with green bonds to support these objectives.

London, Luxembourg & Stockholm: Listing centres for green bond issuance

One of the first sustainable green bond markets was set up in 2015 on the Nasdaq Stockholm with two sustainable green bond segments launched on the Stockholm main market and on Nasdaq First North Bond Market.⁸ To access the segments, issuers need to disclose information on use of proceeds, present a third-party review and report annually until the full allocation of proceeds. In 2018, Nasdaq Stockholm Sustainable Commercial Papers and Nasdaq Stockholm Sustainable Products were also launched, listing sustainable commercial paper and structured products respectively, and highlighting further growth and innovation in the green and sustainable debt markets. Nasdaq Stockholm is the main listing centre for green bonds issued out of the Nordics.

Over the past few years, London and Luxembourg have also established their

role as listing centres for domestic and international bonds, including for green bonds. Both exchanges are home to dedicated green bond segments. For green bonds to access the exchanges' green segments, issuers are required to submit relevant documentation to ensure a degree of transparency with respect to the assets being financed.

The London Stock Exchange green segment is currently home to 95 green bonds listed in several different currencies including INR, SEK and MXN. The green segment offers issuers a flexible range of market models covering both Regulated Market (RM) and Multilateral Trading Facility (MTF). Issuers are required to submit an external review or second party opinion to verify the green nature of the bond.

In 2016, the Luxembourg Stock Exchange launched the Luxembourg Green Exchange (LGX), the first platform worldwide to list exclusively green, social and sustainable bonds. The Luxembourg Stock Exchange is also home to the first Climate Awareness Bond issued in 2007 by the European Investment Bank. LGX listing requirements apply strict eligibility criteria, including pre- and post- issuance reporting.

Milan: the climate-aligned segment and minibonds

Borsa Italiana has also established a dedicated green bond segment in 2017 and lists green and social bonds on both its MOT (electronic fixed-income market)

and ExtraMOT (multilateral trading facility dedicated to bonds) markets.

In common with the LSE, it requires external reviews or second party opinions as part of eligibility criteria for bond listing. Additionally, Borsa Italiana has enabled the identification of so-called climate-aligned bonds through its ExtraMOT PRO, which allows for identification of bonds that are not labelled as green or social but are issued by companies belonging to sectors supporting the transition to a low carbon economy.

ExtraMOT Pro is also the platform where minibonds are listed on the Borsa Italiana. Minibonds are a fixed-income debt instrument for unlisted companies, allowing these companies to access capital markets and diversify their sources of funding from bank credit. 334 minibonds have been issued on the Italian market to date for a total of EUR 16.4 bn, more than 80% of which have an issuance size smaller than GBP 50m.⁹ There is the potential to explore green and social bonds for this market segment and for Milan as a financial centre to combine its expertise around mini- and green bonds.

Paris and Dublin: centres for Sovereign Green Bond Issuance

2017 was an important year for sovereign issuance in the green bond space. In France, the green OAT has played a fundamental role in leveraging green bonds to highlight Paris as a financial centre for sustainability. To date, France has issued the largest sovereign green bond which

has raised just below EUR15bn. The bond proceeds have been used to fund a variety of projects spanning across different sectors such as renewable energy, energy efficiency, transport, land use and adaptation. The French sovereign green bond represents a landmark issuance as it sent a strong signal to the market as witnessed by several other nations following suit during 2017.

France has also played an important role in sub-sovereign green bond issuance, as it is also home to the first local government sustainability bond issued by Ile-de-France back in 2012. The City of Paris has consolidated its commitment to sustainability by issuing a EUR300m sub-sovereign green bond in 2015 aimed at funding projects in low-carbon buildings, transport, renewable energy generation and sustainable agriculture. Other French sub-sovereign sustainability bonds include issuance from Provence-Alpes-Côte d'Azur, Hauts-de-France and Department de L'Essonne. State-owned railway company SNCF and state-backed energy utility company EDF are also key actors in green bond issuance, having issued multiple bonds raising EUR2.6bn and EUR30.4bn respectively for financing of renewable energy production and low carbon transport.

Ireland also came to the market with its first sovereign green bond issuance in October 2018 strengthening Dublin's commitment, as a financial centre, to climate action and sustainability. The green bond is going to finance a wide range of eligible project categories including water and wastewater management, clean transportation, renewable energy and climate change adaptation. Ireland plans to report annually on the proceeds allocation and every two years on impact.¹⁰



Frankfurt: a development bank story

Frankfurt's financial centre green bond story starts the Frankfurt-based giant development bank KfW as a green bond

issuer lead, with 20 green bonds issued since 2014, amounting to more than USD270bn. The green bond proceeds are primarily used to finance renewable energy generation from wind, solar and some hydro and biomass. KfW is committed to transparency, reflected by their quarterly reports on the use of proceeds raised via green issuance and their detailed annual impact reporting.



Zürcher Kantonal Bank & Canton of Geneva: green sub-sovereigns

Zürich and Geneva are using sub-sovereign green bonds to signal

their commitment to green action and sustainability. The Canton of Geneva issued its first local green bond in November 2017 raising USD610m to finance the canton's ten-year investment plan, which includes enhancing energy efficiency in buildings. The Zürcher Kantonal Bank has also issued a green bond in 2018, raising USD324m to finance or re-finance assets such as private, commercial and real estate loans as well as housing cooperatives. Both issuers are committed to report annually on proceed allocation as well as impact.

Opportunities for financial centres & green bonds

Green bonds are an effective instrument for financial centres wishing to strengthen their offering and competitiveness with respect to sustainable finance objectives. Though green bonds are a capital market instrument, they are a good vehicle to introduce some fundamentals of sustainable finance into the financial centre ecosystem: environmental experts and civil society, green definitions, investor engagement and public policy support for wider sustainable finance initiatives.

Different parts of the financial centre ecosystem can play an active role in developing green bond markets: exchanges can develop dedicated green bond listing rules and explore new market segments; central and local governments and development banks can be demonstration issuers; and regulators can implement regulations around disclosure and risk management related to climate change risks.

FC4S Europe members have a significant part to play in catalysing their stakeholders around green bond market development by exploring, through the resources offered by the Network membership and Partners, the following opportunities:

- **Green bond guidance:** FC4S members can consult with their members on the need to develop guidance on green bonds in form of a general guide, guidelines from stock exchanges or regulation from securities regulators. The development of a guide for green bonds could even be commissioned by FC4S members.

- **Green bond training:** FC4S members can convene workshops and training sessions for issuers, investors and verifiers through network partners such as the Climate Bonds Initiative and the Frankfurt School.

Peer-to-peer exchanges can also be organised through the FC4S Europe Network.

- **Sustainable finance committees:** FC4S members can explore the option of convening a dedicated sustainable finance committee or green finance initiative/ taskforce comprising representatives from their stakeholders to develop a common agenda around sustainable finance and engage with regulators and policymakers accordingly.

Endnotes

1 UNEP Inquiry, Corporate Knights (2017): Financial Centres for Sustainability (<http://unepinquiry.org/publication/financial-centres-for-sustainability/>)
2 UNEP Inquiry (2017): Accelerating Financial Centre Action on Sustainable Development (https://docs.wixstatic.com/ugd/eb1f0b_5709d803e0fd49169124afe8e00f3765.pdf)
3 Retail investors can be an important source of sustainable finance given their direct interest in developing sustainable infrastructure in their cities and regions. US green municipal bonds have been successfully issued for the retail market, thanks also to a tax exemption on income from municipal bond investments.
4 For more information visit: https://ec.europa.eu/info/publications/sustainable-finance-technical-expert-group_en
5 Climate Bonds Initiative (2016, 2017, 2018): Scaling up green bond markets for sustainable development; The Role of Exchanges in accelerating the growth of the green bond market; The green bond market in Europe.

6 For more information visit: https://ec.europa.eu/info/publications/180524-proposal-sustainable-finance_en
7 Paris is leading on this front with the implementation of Article 173; several regulators are looking at how to implement the recommendations of the TCFD and the European Commission has proposed a regulation on disclosures relating to sustainable investments and sustainability risks.
8 Nasdaq First North Bond Market is an alternative marketplace which offers issuers more flexible admissions requirements and is therefore well suited for smaller issuers, private placements, and retail bonds
9 www.minibonditaly.it
10 See Sustainalytics (2018): Second Party Opinion Irish Sovereign Green Bond

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