Climate Bonds Initiative

Green Bonds Policy: Highlights from 2017

Public sector green bond action around the world and the major developments expected in 2018.

2017 top five green bond policy developments

1. The year of sovereigns

France kicked off 2017 with a sizeable EUR7bn (USD7.5bn) sovereign green bond. By the end of the year, it had tapped the bond twice more leaving the final total of their sovereign green bond at almost EUR10bn (USD10.7bn) – the largest bond of 2017.

Fiji issued an FJD100m (USD50m) sovereign green bond for climate mitigation and adaptation in November. A smaller bond, but exciting from a diversity perspective: the first from an emerging market and the first in Asia.

Nigeria followed in December with their much-anticipated green bond issuance of NGN10.7bn (USD29 .7m), which marks the first issuance from a planned NGN150bn (USD418.5m) green bond issuance programme. This was the first sovereign green bond to achieve Climate Bonds Certification.

The sovereign green bond issuances in the past year have established a foundation for more governments to come to market with sovereign green deals to raise the capital required to meet official climate targets (Nationally Determined Contributions – NDCs) and priority Sustainable Development Goals. We expect more in 2018.

Benefits of issuing a sovereign green bond

- Raise low-cost capital for low carbon infrastructure
- Signal the country's commitment to low carbon growth strategies
- Attract new investors
- Catalyse development of a domestic green bond market to mobilise private capital for green infrastructure

Country-level and regional guidelines largely aligned with international best practice

The increasing number of country-level and regional guidelines does not mean we are seeing a fragmentation of the green bond market

The guidelines from China, India and ASEAN are all in line with international best practices on the issuance process of green bonds, as set out by the Climate Bonds Standard and Green Bond Principles. While some differences remain in the definition of green at the project level (like the inclusion of certain fossil fuel projects under China's green bond guidelines), in practice most bonds issued against the various country-level guidelines also aligned with international definitions. In China approximately two thirds of green bonds from domestic issuers meet international green definitions.

Work is underway for further global alignment of green definitions

The European Investment Bank and China Green Finance Committee are looking at harmonisation of definitions for green investments between the EU and China. 2017 also saw an increasing amount of green bonds from India, China and other emerging economies issued internationally, several of which certified against the Climate Bonds Standard.

2. Country-level and regional guidelines kick-start local green bond markets

The development of clear guidelines and standards for what is green are a key step to establish the foundation for a green bond market.

India: The Securities and Exchange Board (SEBI) released a final version of their guidelines in May, following consultations with the Finance and New and Renewable Energy Ministries. The guidelines include key sectors for eligible green projects, optional pre-issuance, compulsory post-issuance verification and semi-annual reporting.

China: The China Securities Regulatory Commission (CSRC), which regulates listed companies, issued green bond guidelines in 2017 following the lead of other regulators in 2016. The green definitions are those adopted by the central bank – the People's Bank of China (PBoC) - for the inter-bank bond market, with an extra provision that excludes high-polluting companies that are in conflict with the national planning policy.

The PBoC and CSRC also released joint guidelines for green bond verifiers and verification activities in China. The guidelines will be under the supervision of a new 'Green Bonds Standard Committee', which is currently being set up. The 'Green Bond Assessment and Verification Guidelines (Provisional)' introduce regulatory requirements for verifiers, and essentially act as a verifier licencing scheme, stipulating required qualifications and credentials, verification methods, and reporting requirements. China's scheme is the first time a government regulator has ventured into supervising verifiers. The scheme is broadly modelled on the international Climate Bonds Standard & Certification Scheme.

ASEAN: The ASEAN Capital Markets Forum published the ASEAN Green Bond Standards (AGBS) in November 2017. The standard is aligned with the international Green Bond Principles on the green bond issuance process, and importantly specifically excludes fossil fuel-related projects from being financed.

Other developments from 2017 include green bond guidelines from the Ministry of Environment in **Japan**, the securities regulator OJK in **Indonesia** and green bond listing requirements from **Taipei** and **Johannesburg** Stock Exchanges.

3. Targeted incentives for green bond issuers

2017 has seen the implementation of new forms of financial support from public sector entities. This lowers the initial hurdle for new issuers entering the market and absorbs the additional costs of an environmentally robust issuance.

Singapore: In March, the Monetary Authority of Singapore, the country's central bank, announced their green bond grant scheme that will absorb the full cost of an external green bond review.

Malaysia: In July, the Securities Commission of Malaysia announced a tax incentive scheme for socially responsible (SRI) sukuk, including green sukuk, until 2020. Natural resources, renewable energy and energy efficiency are highlighted as eligible project categories, and the scheme encourages independent review of the green credentials of the sukuk. The move follows the pioneering launch of a SRI sukuk framework by the Securities Commission in 2014.

The green sukuk issuance from Permodalan Nasional Berhad is a great example of how the tax incentive scheme works in tandem with other public sector initiatives to boost the nascent green sukuk market (see box).

China: An additional type of government support seen for the first time in 2017 is China's fast-tracking of green bond issuance approval. Green bonds are given preference over non-green bonds in the bond issuance approval queue, so far mainly at the local level.

4. Public sector issuers set examples for private sector

Public sector green bond issuance in 2017 amounted to approximately USD90bn (see bar chart below). Pioneering issuers included:

Government-backed entities: US Agency Fannie Mae's Green Initiative Programme and transparency around labeling deals was a game changer in 2017 (see Green Bond Highlights 2017). The agency was by far the largest issuer globally with a whopping USD24.9bn of green Mortgage-Backed Securities (MBS) issuance. The greater visibility of MBS from government agencies has huge potential to spur property-backed green bonds, both for existing low carbon buildings and for energy and water efficiency improvements.

State-owned companies: Three Indian state-owned companies issued green bonds which were certified against the Climate Bonds Standard in London in the second half of 2017: India Railway Finance Corporation (USD500m), renewable energy agency IREDA (INR19.5bn) and Power Finance Corporation (USD400m). The string of issuances sets a precedent for India's private sector to follow suit in attracting international capital to the country's massive low-carbon transport and energy expansion through offshore, certified green bond issuance.

Development banks: China Development Bank, one of China's three mammoth policy banks, became the first Chinese public sector entity to issue a Climate Bonds Certified bond (USD1.62bn). As in India, the precedent has now been set for Chinese state-owned enterprises (SOEs) and banks to follow in the development bank's footsteps to raise international capital for their green ambitions.

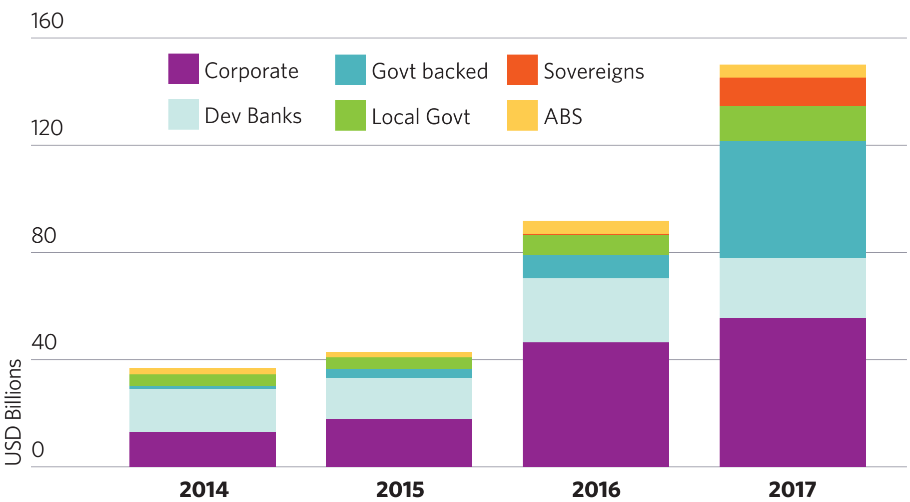
Munis: South Africa continues to lead the way for emerging market cities with a Climate Bonds Certified bond issuance from Cape Town (R1bn), following the first emerging market city bond from Johannesburg back in 2014. The bond proceeds are for the large part refinancing resilient water infrastructure projects, such as water capture, storage and distribution infrastructure, alternative waste treatment plants and flood defences.

Green sukuk: Public sector support creates conditions for rapid market growth

The first-ever green sukuk deal came to market in 2017 with an issuance from Malaysian company Tadeu energy (USD58.5m), following the launch of the country's tax incentive scheme for green sukuk. Quantum solar park followed suit with a USD236m deal, and in November Malaysia's Permodalan Nasional Berhad (PNB), a government-linked investment company, announced the issuance of a l arger RM2bn (USD482m) green sukuk to finance a green building project.

The green sukuk public sector issuance from PNB illustrates the complementarity of different public sector initiatives in supporting the green debt markets. The green sukuk adheres to the recently launched ASEAN Green Bond Standard, the first deal to do so, demonstrating to other potential green sukuk issuers that they can use existing green bond guidelines and standards. PNB's sukuk also complies with the Malaysian Securities Commissions Framework on Socially Responsible Investment sukuk. Malaysia's tax incentive scheme for green sukuk works to make issuance costs lower for green than non-green, making it an attractive choice even before the general issuer benefits of the green label are taken into account.

Future growth potential is massive: Green sukuk combines two of the fastest growing segments of the financial markets – green bonds and Islamic finance. We expect more green sukuk deals in 2018 across more geographies from Malaysia, Indonesia and UAE.



Top issuers of 2017: all public sector entities

1: Fannie Mae: **USD24.9bn**

2: Republic of France: **EUR9.7bn** (USD10.7bn)

3: China Development Bank: **USD4.6bn**

4: European Investment Bank: **USD4.6bn**

5: New York MTA: **USD4.2bn**

5. Public-private collaboration

EU High-Level Expert Group on Sustainable Finance (HLEG) has been working tirelessly in 2017 to present its final recommendations to the European Commission in January 2018. An interim report was released in July 2017 and was subjected to public consultation. Recommendations spanned from the development of a EU Sustainability Taxonomy, climate-related financial disclosure for companies, labels for sustainable investments and environmental risk management. The Commission is committed to proposing its own Sustainable Finance Action Plan in March 2018, building on the final recommendations of the HLEG.

The UK-Brazil Green Finance Partnership was launched as part of the second annual UK-Brazil Economic and Financial Dialogue. The City of London's Green Finance Initiative and the Brazil Green Finance Initiative (previously Brazil Sustainable Market Development Council) will collaborate to support sustainable economic growth in the two countries. Green bond market growth, both at the domestic and international level, is high on the Partnership's agenda.

China's Belt & Road Initiative (BRI) is providing huge investment opportunities for green infrastructure projects after China's President Xi emphasized in 2017 that the initiative needs to be green. Green bonds are expected to become a feature of the financing packages for these projects in 2018.

The Central Banks and Supervisors Network for Greening the Financial System was launched in December and includes eight central banks and financial supervisory bodies from China, Singapore, Mexico, England, France, Germany, the Netherlands and Sweden. Green bonds are likely high on the Network's agenda as all the countries on the list are green bond pioneers.

Three key developments to look forward to in 2018

1. Sovereign green bonds issuance

Several governments have made announcements around sovereign green bond issuance. In Sweden a green bond inquiry commissioned by the Ministry of Finance put sovereign issuance at the top of the list of recommendations that were published in early January 2018. Belgium, Morocco, Kenya, Hong Kong, Indonesia and Argentina have also expressed interest in issuing green sovereigns.

2. Harmonisation of guidelines from financial regulators

Africa: The Nigerian Securities Exchange Commission is finalising its green bond guidelines. Market feedback on a draft of the guidelines is currently being reviewed and a final version is expected in H1 2018. The Nairobi Securities Exchange has also been working on green bond listing which it is looking to publish in 2018.

Asia: In January 2018, Hong Kong Quality Assurance Agency, a government-linked entity, launched a Green Finance Certification scheme. In 2018, we look forward to seeing financial regulators in ASEAN adopting the regional ASEAN green bond standard at the country-level. Indonesia's Financial Services Authority for example has published its own regulation in line with the ASEAN green bond standard.

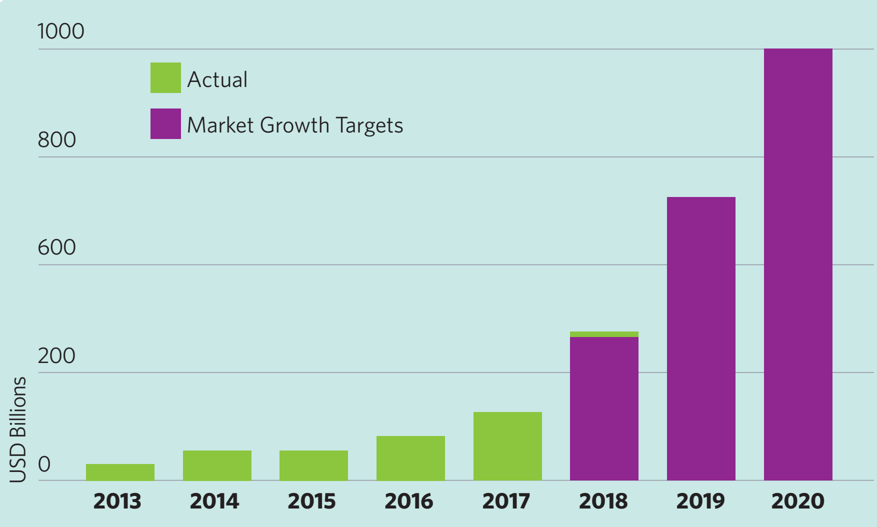
Europe: The launch of a European Taxonomy for Sustainable Finance is expected in H1 2018. The taxonomy is set to define sustainable investments for financial stakeholders and be the basis for future policy support.

3. Additional green bond policy support

More actors are considering additional policy support to rapidly grow the green bond market given the extreme urgency and scale of the climate challenge.

EU: The European Commission is considering lowering capital requirements for lending against energy efficient buildings and low-emission and electric cars. Commissioner Dobromvskis announced that the Commission will be looking into adjusting risk weightings for green investments as part of its 2018 Sustainable Finance Action Plan.

China: The People's Bank of China is exploring the possibility of allowing green bonds as collateral for borrowing from the Central Bank, and the inclusion of exposure to green lending in banks' macro-prudential assessment frameworks.



Big Picture – The 2020 milestone

A large and liquid green bonds market can support countries in achieving the Paris climate targets (NDCs), while supporting economic growth and infrastructure expansion. Global climate leaders have recently set a milestone of USD1 trillion in green bonds by 2020 as one of six urgent steps needed for a low carbon transition and climate-resilient world, avoiding the most immediate threats and severe consequences of climate change to economic growth and infrastructure development.

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