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News Release

Green bonds: Coming of age

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The green bond market turns ten years old this year and is rapidly heading towards adulthood. As it comes of age, this market will be an increasingly critical source of capital for projects that will help the global economy limit the impact of climate change.

It's not been an entirely easy childhood so far. The first-ever "green bond," a EUR 600 million issue in July 2007, was followed by, well, not very much in the same vein for several years. It took until 2013 for green bond issuance to vault the US$10-billion-a-year mark -- and even that is a tiny amount compared with the overall bond market.

Ten years on, however, the baby of the capital markets has grown spectacularly. Over US$ 90 billion was raised by companies and other issuers via green bonds last year – more than double the 2015 amount. That included the first ever sovereign green bond, a EUR 750 million issue by Poland. The total for the first eight months of this year was more than US$75 billion, and included a EUR 7 billion, 22-year green bond by France – a milestone in terms of its size and long tenor - and all the more remarkable because investor demand, at more than EUR 23 billion, far outstripped the size of the offering. Just over 40% of the issuance so far this year has come from Europe, and about one-third from Asia.

Climate change is an urgent threat to the planet, and major injections of capital are required to finance less carbon-intensive technologies and infrastructure. Green bonds are similar to traditional bonds, except the proceeds from their sale are used to finance projects that benefit the environment. Think wind turbines and solar-energy farms. Think low-carbon transport systems. Think technologies that will make buildings – and entire cities -- ever more energy- and water-efficient.

Take the EUR 500 million green bond that HSBC issued in 2015. The proceeds are flowing into 20 projects in 10 countries, including wind farms in Ireland, Germany, Turkey and elsewhere, solar power plans in the Czech Republic, South Africa and Spain, and waste-management facilities in France and the UK.

The green bond market may be a late developer, but it is now critical to financing a lower carbon economy. It enables companies to tap the growing pool of cash globally that is looking for climate-friendly investment opportunities, converting those funds into capital for environmentally sustainable projects.

At present, green bonds still account for less than 1% of the overall global bond market.[1] But here's why we believe the market is rapidly growing up:

First, there have been profound changes in the way businesses, consumers and investors perceive the risks stemming from pollution and rising global temperatures. The 2015 Paris Agreement established an overwhelming global consensus on the need to address climate change. It required the nearly 200 signatories to develop their own national plans to meet the target of limiting the increase in global temperatures to two degrees Celsius or less over pre-industrial times. This has galvanised global green-tech investments and financing.

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1 HSBC Sustainable Financing Newsletter, December 2016 edition
http://www.gbm.hsbc.com/~/media/gbm/campaign/sustainable-financing/edition3-newsletter-2016/sustainable-newsletter-edition3.pdf

Second, technological advances are making more and more low-carbon alternatives (from alternative energy technologies, to electric vehicles and batteries) economically viable. Green investments are increasingly not just ethically but also financially sound.

Third, the authorities in China and India have thrown their considerable weight behind efforts to green their economies. By launching green bonds for the first time in 2015, Chinese and Indian institutions added geographical diversity to a market that had until then been dominated by the likes of Scandinavia, the United States and Britain. Last year, more than US$ 33 billion-worth of Chinese green bonds were issued. That's over one-third of the global total – and up from just US$ 1 billion in 2015. Indian volumes are more modest, at just over US$ 1 billion last year, but the country is likewise going through a paradigm shift in low-carbon technologies.

The increasing momentum behind green bonds means issuers and investors can no longer afford to ignore them.

True, green bonds come with no significant pricing advantage over ordinary bonds, and there is lingering scepticism over the "greenness" of specific bonds. Are proceeds really deployed to finance climate-related or environmental projects? Or are they headed towards projects or companies whose "greenness" is debatable? Who assesses whether a particular issue is as "green" as another? Many investors are still put off by the lack of consistency and transparency on those fronts, while issuers shy away from the extra efforts (and costs) of disclosing, reporting and certifying "green" ventures.

But the extras tend to be overestimated, and progress is being made on standardization and monitoring. For example, Standard & Poor's in April launched a tool designed to evaluate not just *whether* a bond is green, but *how* green it is.

Meanwhile, the advantages of issuing a green bond are substantial – though perhaps not yet as widely recognized as they should be.

For a start, issuing green bonds allows companies to tap the growing demand for such instruments among pension funds, sovereign wealth funds and other investors who are concerned about their portfolios' exposure to high-carbon and unsustainable issuers and activities.

As of early 2016, there were some US$ 23 trillion of assets professionally managed under responsible investment strategies. That's up 25% since 2014, and represents more than a quarter of all professionally-managed assets globally. Likewise, a recent HSBC survey found that two-thirds of global institutional investors want to put more capital into low-carbon and climate-related investments.

What's more, the launch of a green bond allows an issuer to demonstrate they are aware of and preparing for the long-term challenges of global warming. And, by requiring them to identify, minimize and monitor their climate risk profile, it can help them embed low-carbon thinking in their corporate culture and business strategy. Over the long term, this could well create an advantage over less well-prepared companies in terms of valuation and business prospects.

Given what's at stake, the green bond market's coming-of-age can only be welcome. Happy 10th birthday.

HSBC Holdings plc

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