INVESTING WITH IMPACT YEARBOOK

KangaNews

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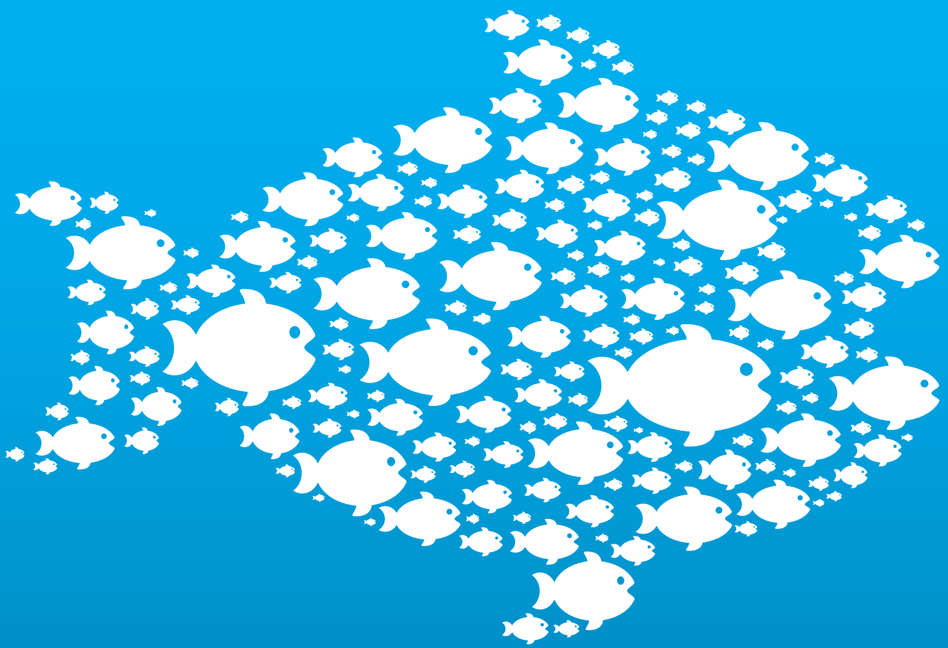
AUSTRALASIAN FIXED INCOME: GLOBAL REACH, LOCAL EXPERTISE

PATH TO TRANSITION

As sustainable finance takes further steps towards the mainstream, market innovation on a massive scale brings bigger goals, more sectors and new instruments into play



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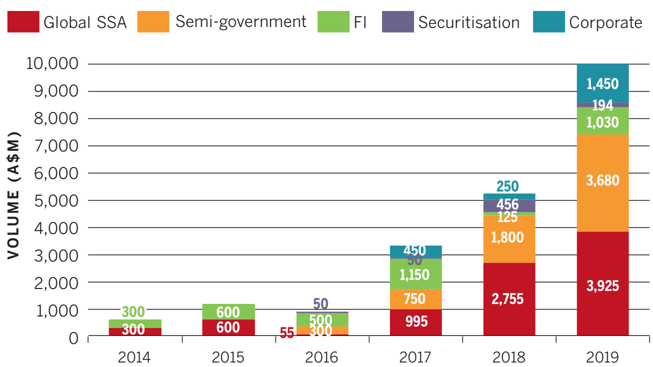
MARKET ANALYSIS

High-grade sectors dominate as Australian dollar GSS issuance surges ahead

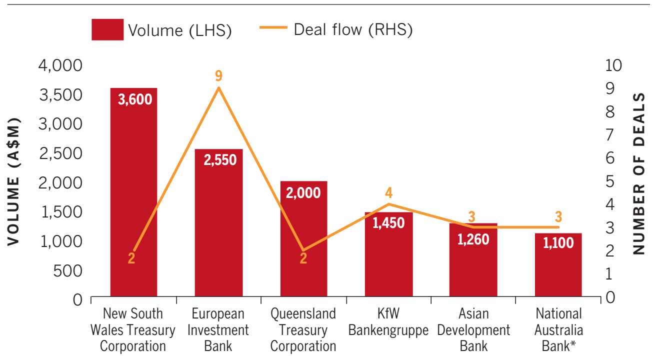
Green, social and sustainability (GSS) bond issuance in the Australian dollar market set a record in 2019 with total volume of almost A$10.3 billion (US$6.7 billion) priced by 31 December. Domestic and international high-grade issuers dominated deal flow, though the corporate sector also took a step forward (see charts 1 & 2). Green bonds continued to provide the bulk of supply (see chart 3).

CHART 1. AUSTRALIAN DOLLAR GSS ISSUANCE BY SECTOR



SOURCE: KANGANEWS 31 DECEMBER 2019

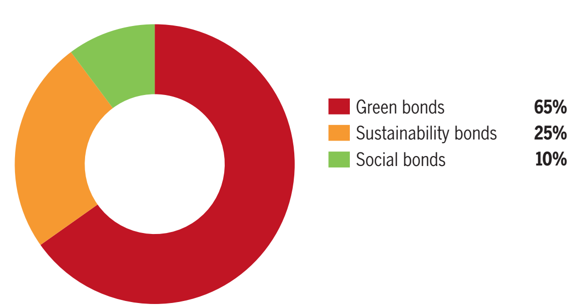
CHART 2. LARGEST AUSTRALIAN DOLLAR GSS BOND ISSUERS



* Volume includes one RMBS tranche

SOURCE: KANGANEWS 31 DECEMBER 2019

CHART 3. MAKEUP OF AUSTRALIAN DOLLAR GSS ISSUANCE, 2019



SOURCE: KANGANEWS 31 DECEMBER 2019

TIMELINE: AUSTRALIAN DOLLAR GSS ISSUANCE BREAKTHROUGHS

April 2014
First green bond (World Bank, A$300 million 2019)

December 2014
First green bond from domestic issuer (National Australia Bank, A$300 million 2021)

April 2016
First green securitisation tranche (flexigroup, A$50 million)

July 2016
First domestic semi-government green bond (Treasury Corporation of Victoria, A$300 million 2021)

March 2017
First social bond (National Australia Bank, A$500 million 2022 gender-equality bond)

March 2017
First corporate green bond (Investa Office Fund, A$150 million 2024)

July 2017
First sustainability bond (Australian Catholic University, A$200 million 2027)

February 2018
First green RMBS tranche (National Australia Bank, A$300 million)

November 2018
Largest GSS bond* (New South Wales Treasury Corporation, A$1.8 billion 2028)

September 2019
First bank Kangaroo green bond (Mitsubishi UFJ Financial Group A$500 million 2024)

November 2019
First corporate Kangaroo green bond (NextEra Energy, A$500 million 2026)

*Equal largest as of 31 December 2019 – TCorp issued another A$1.8bn in November 2019.

SOURCE: ANZ 21 NOVEMBER 2019

SECTOR ANALYSIS

Issuance format broadens as semi-governments lead GSS growth

Semi-government issuers provided more than a third of 2019's total supply of Australian dollar green, social and sustainability bonds in 2019, including debut and follow-up deals from the market's only programmatic social-bond issuer and a jumbo offering from TCorp.

Funding constraints and issuer preferences have so far kept supply limited, however – and only four issuers have brought green, social and sustainability bond (GSS) deals to market (see chart 1).

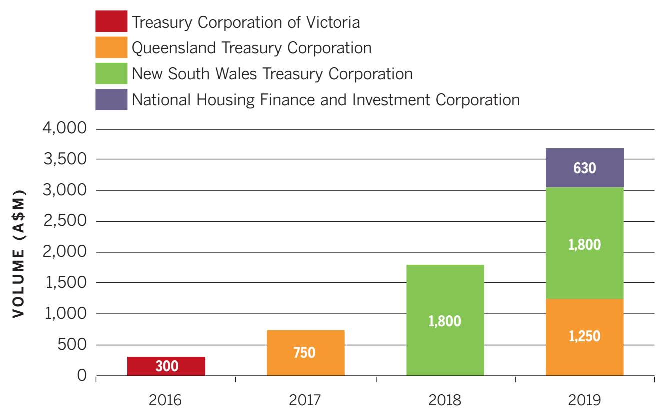
Arguably the biggest change in the market in 2019 was diversification of issuance type (see chart 2). National Housing Finance and Investment Corporation expects all its debt funding to be in the form of social bonds, while New South Wales Treasury Corporation transitioned to sustainability-bond issuance, having made its GSS debut in 2018 with a green bond.

Queensland Treasury Corporation also undertook its second green-bond transaction in 2019. The quantum of issuance from repeat issuers has made the semi-government space a key market for domestic investors seeking exposure to GSS product.

Deal sources believe it is a key sign of market maturity that semi-government borrowers can rely on the GSS bond market not only for repeat issuance but for a meaningful contribution to higher overall debt requirements.

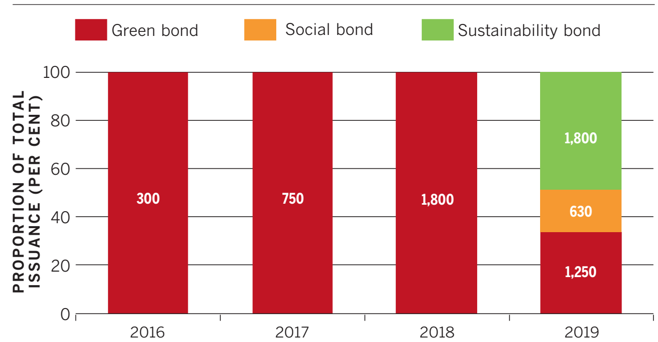
TCorp's benchmark volume across two products labelled differently is a further evolution, and the issuer says it is eager to explore the possibility of increasing the liquidity of its sustainability bond via syndicated increase.

CHART 1. AUSTRALIAN DOLLAR SEMI-GOVERNMENT GSS ISSUANCE



SOURCE: KANGANEWS 31 DECEMBER 2019

CHART 2. MAKEUP OF AUSTRALIAN DOLLAR SEMI-GOVERNMENT GSS ISSUANCE



Bar labels are A$ million.

SOURCE: KANGANEWS 31 DECEMBER 2019

ISSUER INSIGHTS

FIONA TRIGONA
HEAD OF FUNDING AND BALANCE SHEET
NEW SOUTH WALES TREASURY CORPORATION

"We initially expected the deal to be smaller than the previous one as it included social assets, but it didn't make a difference in the end. Investors were very keen: they wanted to see assets apart from just green assets, they wanted to see social outcomes and they wanted to see them reported on."

NATHAN DAL BON
CHIEF EXECUTIVE
NATIONAL HOUSING FINANCE AND INVESTMENT CORPORATION

"We are looking to build a new asset class in the Australian debt capital market with bonds backed by social housing. It was very encouraging to see a diverse group of investors take an interest in our inaugural deal."

Semis take centre stage

Green, social and sustainability bond issuance was a main talking point at the annual government-sector funding roundtable KangaNews hosted in Sydney in January 2019. In this extract from the event, funding executives explain the value of the asset class – and why it is not used more regularly.

PARTICIPANTS
- **Vince Cinquina** Head of Financial Markets WESTERN AUSTRALIAN TREASURY CORPORATION
- **Jose Fajardo** Head of Funding and Liquidity QUEENSLAND TREASURY CORPORATION
- **Andrew Kennedy** Director, Treasury Services SOUTH AUSTRALIAN GOVERNMENT FINANCING AUTHORITY
- **Justin Lofting** General Manager, Treasury TREASURY CORPORATION OF VICTORIA
- **Rob Nicholl** Chief Executive AUSTRALIAN OFFICE OF FINANCIAL MANAGEMENT
- **Katherine Palmer** Senior Manager, Funding and Balance Sheet NEW SOUTH WALES TREASURY CORPORATION

MODERATOR
- **Laurence Davison** Head of Content and Editor KANGANEWS

DAVISON Treasury Corporation of Victoria (TCV) launched the green-bond market for Australian semi-governments in 2016, Queensland Treasury Corporation (QTC) increased deal volume with its debut and – in 2018 – New South Wales Treasury Corporation (TCorp) took the sector to a new level of volume. How have green-bond strategy and capacity developed since the first issuers debuted?

■ **LOFTING** We had a pool of around A$2 billion (US$1.4 billion) of suitable assets when we issued our green bond in 2016 but we didn't need A$2 billion of funding. The reason we haven't been back to the market is the same: we haven't needed a significant amount of funding in the last few years. There is capacity to issue more under the green-bond programme, though.

At the same time, our transaction was the first from our sector and there was limited demand at the time. The TCorp deal reflects how much this has developed. Even though 'dark-green' investment is still limited, other investors could still participate because the TCorp transaction was big enough to create a liquidity point for them. Our green bond was a bespoke deal of interest primarily to specialist green investors.

■ **FAJARDO** When we issued our green bond we had an asset pool of only A$1 billion so there was a constraint on the volume we could issue. This has now grown to more than A$4 billion – so there is certainly capacity, although there are scale limitations because of the pool of assets required.

On the demand side, I don't believe dark-green demand really grew between our trade and TCorp's [debut]. It is growing in Europe but I think we would only access this with a euro-denominated deal.

■ **PALMER** New South Wales (NSW) state-government spending on infrastructure is roughly A$90 billion over the forward estimates with A$7 billion each on education and health. As part of the usual remit for semi-government spending is that it go toward assets and projects that have a social outcome, there is potential for inclusion of these assets in a social or sustainability bond.

The challenge is that social bonds haven't evolved as much on recognised standards. The green-bond standards are much more developed. If we go out with a social bond under the TCorp framework, we need to make sure our assessment of a social asset meets the broad expectations of potential investors. The UN Sustainable Development Goals are probably the best way to do this.

DAVISON Could green bonds become a liquid curve alongside mainstream programmes?

■ **FAJARDO** QTC has benefited from having large, liquid benchmark lines. The message from investors is that they like this depth, and we see green bonds as a complement to this. We have become a programmatic issuer of Climate Bonds Initiative-certified green bonds, which streamlines the process for future issuance.

■ **PALMER** Similar to QTC, the focus for TCorp is still on highly liquid benchmark lines. But the diversification angle is important. Even if the dark-green investor set remains small, the ability to tap into this sector is one of the advantages of green-bond issuance.

DAVISON What do issuers that have not yet entered the GSS bond market think about the asset class?

■ **NICHOLL** The Australian Office of Financial Management has no current plan to issue green bonds but it is increasingly clear to me that European fund managers in particular have growing mandates for environmental, social and governance (ESG) investments. My guess is that at some point in the future all sovereigns will have to look at meeting these mandates in some way or another.

■ **CINQUINA** [TCorp's November 2018 green bond] was certainly an impressive trade and I was also impressed to hear that TCorp found 15 new investors. We are looking at the sector but we don't actively have projects in train that would result in issuance in the near future.

■ **KENNEDY** Our long-term strategy when it comes to ESG factors and bond issuance has been to seek to have the entire programme certified, rather than focus on one particular bond issue. This will continue to be our message and key strategy – one we aim to deliver. •

SECTOR ANALYSIS

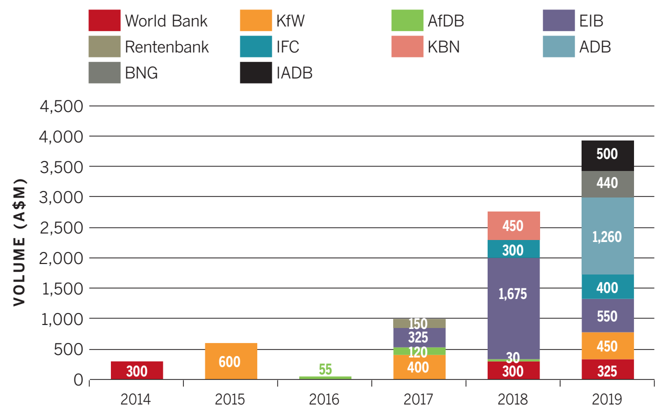
SSA sector out in front

Global supranational, sovereign and agency (SSA) issuers once again provided the backbone of Australian dollar green, social and sustainability bond issuance in 2019. The sector printed nearly A$4 billion (US$2.7 billion) of aggregate deal volume in the year to 31 December (see chart).

A total of 10 SSA issuers have brought green, social and sustainability (GSS) Kangaroo deals to market since World Bank made its debut in April 2014. Seven borrowers accessed the market in 2019 – the most active being Asian Development Bank, which issued A$1.3 billion in total including the Kangaroo market's first A$1 billion GSS deal.

GSS issuance has also allowed a clutch of smaller SSA issuers – including BNG Bank in 2019 – to access benchmark-sized funding in the mid part of the curve, which is otherwise

CHART 1. KANGAROO GSS ISSUANCE



SOURCE: KANGANEWS 31 DECEMBER 2019

often unavailable to these names in the Kangaroo market. SSAs including Inter-American Development Bank and International Finance Corporation, meanwhile, have added diversity to the type of GSS bond issued in Australia.

TRANSACTION HIGHLIGHTS

Issuer: **Asian Development Bank**
Issuer rating: **AAA/Aaa/AAA**
Pricing date: **8 January 2019**
Maturity date: **17 January 2024**
Format: **green bond**
Volume: **A$1 billion**
Margin: **42bp/s-q swap**
Lead managers: **Deutsche Bank, Nomura, TD Securities**

★

Issuer: **International Finance Corporation**
Issuer rating: **AAA/Aaa**
Pricing date: **10 January 2019**
Maturity date: **15 March 2023**
Format: **social bond**
Volume: **A$400 million**
Margin: **40bp/s-q swap**
Geographic distribution: **70% Asia, 26% Australia, 4% Americas**
Lead managers: **CommBank, Deutsche Bank, J.P. Morgan (JPM)**

★

Issuer: **Inter-American Development Bank**
Issuer rating: **AAA/Aaa**
Pricing date: **10 April 2019**
Maturity date: **23 April 2024**
Format: **education, youth and employment bond**
Volume: **A$500 million**
Margin: **35bp/s-q swap**
Geographic distribution: **50% Australia, 37% Asia, 11% EMEA, 2% Americas**
Distribution by investor type: **50% asset manager, 30% central bank/official institution, 10% bank, 10% insurance**
Lead managers: **ANZ, CommBank, JPM**

★

Issuer: **BNG Bank**
Issuer rating: **AAA/Aaa/AAA**
Pricing date: **29 May 2019**
Maturity date: **26 November 2025**
Format: **sustainability bond**
Volume: **A$300 million**
Margin: **50bp/s-q swap**
Geographic distribution: **77% Australia, 15% Asia, 8% EMEA**
Distribution by investor type: **62% asset manager, 31% bank, 7% central bank/official institution**
Lead managers: **Nomura, RBC**

ISSUER INSIGHTS

ANTHONY RUSCHPLER
TREASURY SPECIALIST
ASIAN DEVELOPMENT BANK

"We do not think we would have achieved the same outcome for a regular outing. Not only did most of the key domestic SRI buyers participate but so did several offshore accounts that have been absent from the Kangaroo market for a number of years."

DOMINIKA ROSOLOWSKA
CAPITAL MARKETS OFFICER, SUSTAINABILITY FUNDING
EUROPEAN INVESTMENT BANK

"From a sustainability funding perspective, the Australian market has definitely become strategic for us. Issuance will naturally be subject to demand but we are quite confident in the increasing interest in GSS products. We would like to come back to this market on a regular basis and provide liquidity in existing lines."

LARS AINSLEY
SENIOR MANAGER, NEW ISSUES
KFW BANKENGRUPPE

"When we issued our first green bond in Australian dollars, the market was in its infancy. Since then, issuance volume for GSS bonds in Australia has reached new heights and numerous issuers have 'joined the band'. The sustainable-finance roadmap for Australia and New Zealand paves the way for continued development of what is still a relatively nascent market segment."

GÜNTHER BRAUNIG
CHIEF EXECUTIVE
KFW BANKENGRUPPE

"In the race to a zero-carbon world, we have a long way to go and not much time left to get there. In this context, including transition in green bonds as well as strictly zero-carbon assets is a political compromise but one I hope the green-bond community should be able to live with."

LAURA FAN
HEAD OF FUNDING
INTER-AMERICAN DEVELOPMENT BANK

"We had domestic and international investor participation in our Kangaroo EYE [education, youth and employment] bond from accounts that had never before bought an Inter-American Development Bank bond."

ANDREA DORE
HEAD OF FUNDING
WORLD BANK

"As investors focus more on issuers' overall sustainability credentials, we can move beyond looking only at a small part of an issuer's activities to considering the ESG [environmental, social and governance] profile and purpose of the issuer as a whole."

MARCIN BILL
SENIOR FINANCIAL OFFICER
INTERNATIONAL FINANCE CORPORATION

"In my view, there is a structural deficiency among investors that focus on green bonds rather than looking at overall issuer profiles. Only those that really care about this will push the discussion forward and, therefore, at best they will see green bonds as a transitory token to raise awareness, among polluting industrials for instance."

WILLEM LITTEL
SENIOR MANAGER, CAPITAL MARKETS AND INVESTOR RELATIONS
BNG BANK

"A common global language has been in the making for some time already. The ICMA [International Capital Market Association] Green Bond Principles are the best example of this but there are more initiatives. The EU taxonomy is in this respect a logical and valuable addition to market development and will eventually evolve into a common language."

SECTOR ANALYSIS

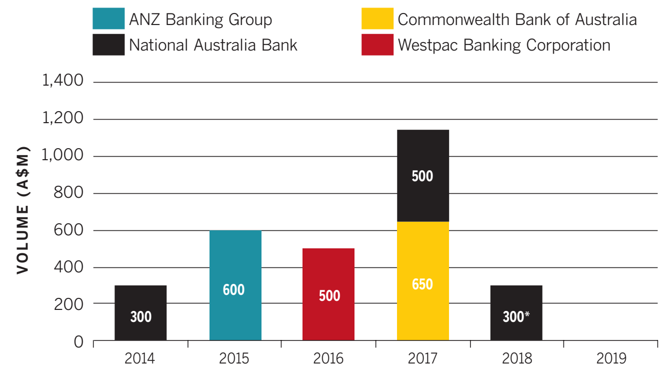
Australian financials take a breather in GSS issuance

As recently as 2017, financial institutions (FIs) were the largest issuer sector in the Australian green, social and sustainability (GSS) bond market. Domestic FI names were virtually silent in 2019, with issuance dominated by offshore banks issuing Australian dollar deals.

Teachers Mutual Bank (Teachers Mutual) priced a A$100 million (US$67.7 million) deal off its ethical bond programme in October. Volume came in the form of a A$500 million debut print from Mitsubishi UFJ Financial Group off the bank's EMTN programme and the same volume issued by OCBC Sydney Branch.

Australia's big four banks were absent from virtually all global GSS markets in 2019, except for ANZ Banking Group's €1 billion (US$1.1 billion) UN Sustainable Development Goals bond print in November (see chart 1).

CHART 1. AUSTRALIAN DOLLAR GSS ISSUANCE BY DOMESTIC MAJOR BANKS



* Green RMBS tranche.

SOURCE: KANGANEWS 31 DECEMBER 2019

A quiet year for GSS issuance does not mean Australian banks' focus on environmental, social and governance factors in the funding and lending arena has dropped, however. Other initiatives include the launch of ethically certified deposit products – including from Teachers Mutual and Westpac Banking Corporation – and, perhaps most significantly, the emergence of sustainability-linked loans (see p13).

TRANSACTION HIGHLIGHTS

Issuer: **Teachers Mutual Bank**
Issuer rating: **BBB/Baa1**
Pricing date: **16 October 2019**
Maturity date: **28 October 2022**
Format: **ethical bond**
Volume: **A$100 million**
Margin: **90bp/3m BBSW**
Indicative margin: **90-95bp/3m BBSW**
Lead managers: **National Australia Bank, Westpac Institutional Bank (Westpac)**

★

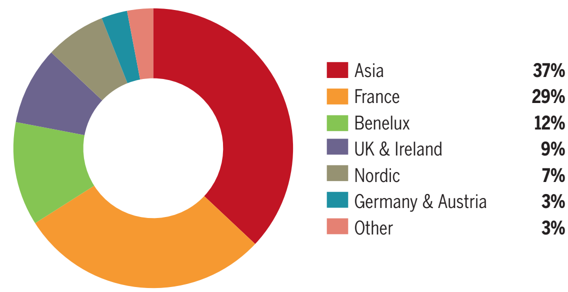
Issuer: **Mitsubishi UFJ Financial Group**
Issuer rating: **A-/A1/A**
Pricing date: **24 September 2019**
Maturity date: **1 October 2024**
Format: **TLAC-eligible green bond**
Volume: **A$100 million fixed & A$400 million FRN**
Margin: **125bp/s-q swap & 3m BBSW**
Indicative margin: **128bp/s-q swap & 3m BBSW**
Geographic distribution: **60% Australia, 39% Asia, 1% EMEA**
Distribution by investor type: **67% asset manager, 28% bank, 5% other**
ESG distribution: **17% dark-green, 48% light-green, 35% other**
Lead managers: **ANZ, Morgan Stanley, MUFG Securities, National Australia Bank, Westpac**

★

Issuer: **ANZ Banking Group**
Issuer rating: **AA-/Aa3/AA-**
Issue rating: **BBB+/Baa1/A+**
Pricing date: **15 November 2019**
Call date: **21 November 2024**
Format: **tier-two UN SDG bond**
Volume: **€1 billion**
Final book volume: **€2.7 billion**
Margin: **140bp/mid-swap**
Indicative margin: **160bp/mid-swap**
Geographic distribution: **see chart 2**

Distribution by investor type: **36% central bank/official institution, 34% asset manager, 24% insurer/ pension fund, 6% bank**
Lead managers: **ANZ, Barclays, BNP Paribas, HSBC, Societe Generale**

CHART 2. ANZ UN SDG DEAL GEOGRAPHIC DISTRIBUTION



SOURCE: ANZ 21 NOVEMBER 2019

SECTOR INSIGHTS

JUNSE YAMADA
VICE PRESIDENT, OFFICE OF THE CFO
MITSUBISHI UFJ FINANCIAL GROUP

"From what we have seen, TLAC deals from other large Japanese banks in Australian dollars have tended to print 7-11 basis points back of US dollars. We were very pleased to print flat to, or even slightly inside, our US dollar curve. We printed A$500 million from a book that was close to A$1 billion and this gives us a good feeling about future deal outcomes."

MOSTYN KAU
HEAD OF GROUP FUNDING
ANZ

"There is a lot of motivation to facilitate funding in this space. While ANZ has in no way been funding constrained over recent years, SDG bonds increase diversification into a growing investment pool and they increase the prominence of lending to environmentally sustainable projects. Even though the product mix of our funding requirement has changed, the focus on SDG issuance remains."

JOSH SIFE
DIRECTOR, CAPITAL MARKETS ORIGINATION
NATIONAL AUSTRALIA BANK

"While the MUFG Group deal tapped into dark-green money, the ESG component gave additional profile, which drove light-green and vanilla investors to participate as well. From the roadshow, there was an eagerness from investors to get more involved in green bonds – and this transaction gave them the opportunity to do so."

ANNA STEWART
HEAD OF CORPORATE SUSTAINABILITY
ANZ

"In the past few years, sustainability has gone from sitting primarily in corporate affairs, associated with governance and reporting, to something the business is delivering as part of its overall strategy. In a company of 40,000 people, sustainability can't just be the responsibility of a few – it needs to be part of everyone's business."

DIDIER VAN NOT
GENERAL MANAGER, CORPORATE AND INSTITUTIONAL BANKING
WESTPAC INSTITUTIONAL BANK

"We have moved far too slowly so it is timely that the [Australian Sustainable Finance Initiative] roadmap has come to life now. In the next 12-18 months, we hope we'll be able to outline some recommendations that can not only have a positive impact on the debate in Australia but also drive policy, legislation and regulation."

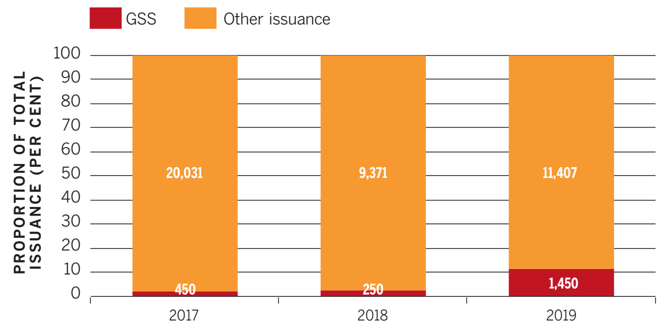
SECTOR ANALYSIS

Woolworths and Sydney Airport headline corporate Australia's sustainable-debt year

Green, social and sustainability (GSS) bonds in 2019 made up more than 10 per cent of aggregate Australian dollar deal flow from corporate issuers for the first time (see chart 1). Among the issuance highlights were Woolworths becoming the first local retail issuer, Macquarie University being the first local corporate to return to the GSS market, and the first corporate Kangaroo GSS bond – from NextEra Energy (see chart 2).

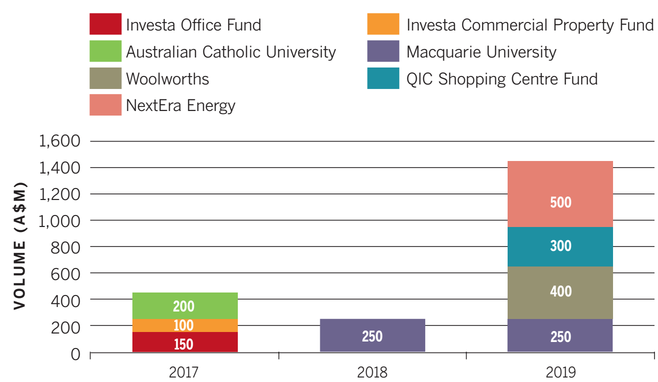
A bigger development for Australian corporate borrowers, however, could be the sustainability-linked loan (SLL). Australia's first such facility was an A$50 million bilateral loan for Adelaide Airport, written in December 2018 with ANZ as lender. The market went to a new level in May 2019, when Sydney Airport closed a fully syndicated facility for A$1.4 billion. ANZ and BNP Paribas were sustainability coordinators and joint bookrunners. AGL Energy and Queensland Airports now also have SLLs.

CHART 1. GSS BONDS AS A PROPORTION OF TOTAL AUSTRALIAN DOLLAR CORPORATE ISSUANCE



SOURCE: KANGANEWS 31 DECEMBER 2019

CHART 2. AUSTRALIAN DOLLAR GSS BOND CORPORATE ISSUERS



SOURCE: KANGANEWS 31 DECEMBER 2019

ISSUER INSIGHTS

DAVID MARR
CHIEF FINANCIAL OFFICER
WOOLWORTHS

"As a company, we have spent a lot of time and money on environmental initiatives so we thought that if the opportunity was there for a financing that aligned with those it would be one we should explore."

BLÁTHNAID BYRNE
GROUP TREASURER
AGL ENERGY

"Banks have their own internal mandates and challenges, in some cases, to justify why they continue to support a borrower. It is on the borrower to show what steps it is taking toward transitioning or 'greening' itself."

AMELIA EVANS
CHIEF FINANCIAL OFFICER
QUEENSLAND AIRPORTS

"Our approach to sustainability-linked loan funding was quite flexible. There are a lot of products in the market, so it was about finding the right one to match Queensland Airports' needs. We have an ESG framework that includes targets for carbon-emissions reduction and the loan was built on the back of this."

SLLs take off in Australia

As Australia's first fully syndicated sustainability-linked loan (SLL) borrower, Sydney Airport attracted significant attention during 2019. The airport's group treasurer, Michael Momdjian, shared insights with *KangaNews* on several occasions – including after loan pricing and at two separate roundtables co-hosted by ING Bank and ANZ.

How did this transaction come to be and what gave the company the confidence to become the first mover in this fledgling format?

We kicked off conversations with lenders in late February and formally launched the transaction in late April, with the SLL delivered under an accelerated timetable in May.

We looked at our debt portfolio with the aim of refinancing our bank-debt facilities well in advance of maturity. We started with a regular bank-debt refinancing process before overlaying the SLL element.

We have been looking at sustainable-financing options for many years. While we have implemented a number of green initiatives, we haven't been able to identify a critical mass of green investment to fund or refinance by way of a green bond or loan.

The emergence of SLLs as a more flexible alternative to use-of-proceeds products, and the timing of our bank-debt refinancing, brought the stars into alignment.

What was the response from your banking syndicate to the decision to market a general refinancing first and then to tell lenders it would be an SLL?

Strategically, we wanted to make sure we achieved the best possible base price before introducing the concept of a sustainability-linked discount.

Many of our lenders were quite excited when we introduced the SLL element and several proactively reached out with details of their banks' sustainability funding targets. In fact, we were significantly oversubscribed from our existing lender group alone. We saw alignment between introducing the sustainability element and the banks' own objectives.

Other banks were eager to be brought on the journey so they could learn from our transaction with a view to marketing or actively participating in similar deals from other issuers in the future.

Can you share some detail about the sustainability structuring aspects of the transactions?

Our loan creates a direct two-way link between our sustainability performance and funding costs. Pricing marginally decreases or increases depending on our sustainability performance over time.

Incorporating a pricing penalty provides real skin in the game. It enhances the credibility of our loan while incentivising management to maintain our current sustainability performance, at an absolute minimum.

What is the potential scale of financing based on holistic scoring of sustainability performance, such as SLLs, versus the use-of-proceeds funding we see in, for instance, the green-bond market?

The potential scale of financing based on holistic scoring of sustainability performance is massive. We are not currently suited to use-of-proceeds sustainable finance, given we lack a critical mass of green investment to fund or refinance. SLLs provide an opportunity to engage in this space.

This very much seems to be the case for many other issuers that have reached out to us following our SLL transaction. Aside from the flexibility of holistic scoring, it is worth noting that products such as SLLs offer other unique benefits such as the potential for a direct and transparent pricing discount or penalty.

We will, however, continue to investigate ways in which we can issue use-of-proceeds-based sustainable funding, especially since our balance sheet primarily comprises long-dated bonds.

As the market evolves from use of proceeds to sustainability scoring at borrower level, one would have to assume the process of agreeing on performance parameters, and assessing and reporting performance, will become more complex. Is this a fair assessment?

The fact that we have a standalone sustainability function and publish a highly comprehensive sustainability report annually made it much easier to establish our SLL and agree on associated targets.

Furthermore, engaging Sustainalytics as an independent third party somewhat outsources assessment and allows us to focus on delivering those initiatives that enhance sustainability performance, rather than on administering our loan.

Does Sydney Airport believe it has a role in helping its peers make the move to sustainability-linked debt funding?

It is one thing to give yourself a pat on the back. But it is another to sit with other corporates and share aspects of your strategy and process to try to develop the product. It would be different if we were all closed to these sorts of conversations. But I think we are all in this together and can all add value, whether through use-of-proceeds bonds or an SLL. Having the conversation is as important as doing the deal. •

SECTOR ANALYSIS

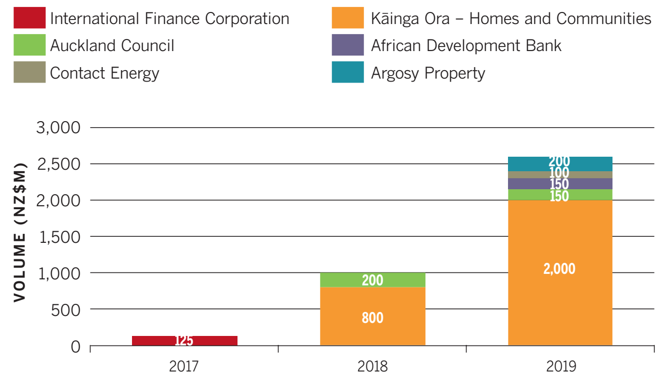
Kāinga Ora takes the lead in New Zealand's jumbo GSS year

Kāinga Ora – Homes and Communities, the issuer formerly known as Housing New Zealand, took a clear lead in New Zealand dollar green, social and sustainability (GSS) bond issuance in 2019. But its wellbeing-bond issuance was not the only breakthrough in a market that is starting to establish its credentials.

Of the NZ$2.6 billion (US$1.7 billion) total GSS issuance in 2019, Kāinga Ora – Homes and Communities was responsible for no less than NZ$2 billion (see chart). The issuer rebranded all its issuance as "wellbeing bonds" in time for its latest transaction, in September, in order to align its debt programme with the New Zealand government's wellbeing budget.

Global placement of New Zealand dollar bonds has been difficult in 2019 as the official cash rate has fallen and the currency has lost some of its appeal to international investors. This has led to a challenging year for the Kauri market, in GSS format and mainstream bonds, and has also required Kāinga Ora – Homes and Communities to rely largely on its home investor base for wellbeing-bond placement (see table).

NEW ZEALAND DOLLAR GSS BOND ISSUANCE



SOURCE: KANGANEWS 31 DECEMBER 2019

KĀINGA ORA – HOMES AND COMMUNITIES DEAL DISTRIBUTION

PRICING DATE	MATURITY DATE	DEAL VOLUME (NZ$M)	DISTRIBUTION: NZ (PER CENT)	DISTRIBUTION: OFFSHORE (PER CENT)	NO. OF INVESTORS
1 Jun 18	12 Jun 23	250	89	11	17
1 Jun 18	12 Jun 25	250	87	13	19
12 Oct 18	12 Jun 23	50	99	1	7
12 Oct 18	18 Oct 28	250	86	14	15
28 Mar 19	5 Oct 26	500	79	21	20
11 Sep 19	12 Jun 25	425	95	5	13
11 Sep 19	28 Oct 28	175	95	5	10

SOURCE: KĀINGA ORA – HOMES AND COMMUNITIES 17 SEPTEMBER 2019

MARKET INSIGHTS

LOUISE TONG
HEAD OF CAPITAL MARKETS AND TAX
CONTACT ENERGY

"With more supply there is likely to be more incentive for institutional investors to dedicate funds to green products. Ultimately, though, institutional investors are responding to demands from their clients and society in general, so it is reflective of a broader push to invest in outcomes that are good for society."

MATTHEW WALKER
CHIEF FINANCIAL OFFICER
AUCKLAND COUNCIL

"With Auckland Council's first green-bond foray, there were a number of questions on the definition of a green bond on the roadshow. This time around, there was greater understanding and acceptance of green as an asset class. Investors have progressed a few steps [and] the local market's understanding and engagement are clearly maturing."

JASON PARIS
CHIEF EXECUTIVE
VODAFONE NEW ZEALAND

"We tick all the ESG boxes but it ultimately starts with our purpose. We won't get to attract the next generation of New Zealanders who are going to transform this country with technology for good if we don't have a clear purpose."

Programme evolution for Kāinga Ora – Homes and Communities

KangaNews has tracked Kāinga Ora – Homes and Communities (Kāinga Ora) from before its return to the bond market and throughout its evolution as one of New Zealand's flagship issuers. Sam Direen, the issuer's Wellington-based treasurer, has always highlighted environmental, social and governance concerns as a core component of the programme. He shares insights with *KangaNews*.

Kāinga Ora is the clear market leader when it comes to green, social and sustainability (GSS)bond issuance in New Zealand, with the biggest volume and largest number of deals issued. Do you think your lead might persuade others to get involved?

The GSS bond market has been developing slowly in New Zealand. But I believe it could be on the cusp of change – and we see an opportunity to help drive this evolution.

Corporate New Zealand is focused on environmental, social and governance (ESG) matters, and positive outcomes. If opportunities to link to financing emerge, and demonstrate consistency, more issuance should come.

We have been asked questions about the mechanics of our sustainability programme by corporate treasurers, although these questions have largely been focused on treasury-specific matters such as financial costs and compliance.

What made it possible for Kāinga Ora to take the lead?

We view any compliance as an opportunity to be accountable and to demonstrate our commitment to ESG. It needs a committed board and positive intent. But the market has matured and so requirements, as we see them, are not onerous.

The challenge can be quantifying the benefits of labelled issuance internally. The key is to communicate these in a qualitative way such that the positive implications for other parts of the business are obvious.

Our commitment to contract all new homes to Homestar 6 standards from 1 July 2019 is a good example of this. Since communicating this intention to investors, the business has been busy ensuring we honour this commitment. Very recently, we confirmed that all our construction panellists have been advised of the new contract forms, with apartments to follow shortly.

There is commercial discipline in being able to say we are committed, while at the same time we are aware that investors are going to expect sustainability considerations from issuers. We understand that sustainability issuance doesn't suit the profile of every organisation in New Zealand. But we hope that if we tell our story it will resonate.

The most recent development has been the revision of Kāinga Ora's programme to align with the government's wellbeing budget. What was the thinking here?

We could clearly see the alignment between our activities and the wellbeing agenda of the government. Updating the framework to reflect this alignment more explicitly made it a natural progression in the evolving space of ESG financing.

We hope this initiative further highlights to the market how core the activities of Kāinga Ora are to government policy. We have a lot of indicators of the social impact of Kāinga Ora's activities, many of which align with what has been defined in the living standards framework. Looking forward, we plan to work with Treasury and other public-sector entities to develop additional impact measures that are clearly related to improved wellbeing.

Selling New Zealand dollar bonds abroad was tough in 2019. Are you happy with the development of the Kāinga Ora investor base, including offshore?

In our last deal, the book built solidly through the New Zealand session but flattened during the Asian and European days. The feedback we received was that some offshore accounts are not currently adding to New Zealand dollar positions, while others are waiting for lines to increase before participating.

We are a developing issuer and know of several investors that are in the process of establishing credit lines. So we are confident we will see increased diversification of our investor base over time.

Does issuing in GSS bond format help the offshore investor-relations task?

We undertook investor relations in Korea and Japan during 2019. While ESG does not yet appear to be driving investment decisions, it's fair to say it is becoming more of a focus for the investors we met, compared with the same time in 2018. In 2019, we proactively mentioned ESG during some meetings but investors asked us about it first in others.

It is significant, for instance, that Japan's Government Pension Investment Fund is making a strategic commitment to this area and it is not surprising that Japanese investors might be considering following this lead. On this basis, we hope to see more demand from the region over time. •

LAURENCE DAVISON
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Will the smoke clear?

Transition is the theme of the day in global sustainable debt, and Australian capital markets are adopting the idea that funding environmental and social evolution across the economy is the next frontier of development. But they are hamstrung by retrograde government behaviour – especially in the environmental space.

If you ask any sustainable-finance professional in Australia about public policy in the context of their area of expertise, the likely response will be a roll of the eyes and a request that whatever they say stay off the record. In short, everyone knows that having a government that refuses to acknowledge the reality of climate change makes everyone's lives unnecessarily harder.

This is a shame, because the mood internationally – or at least in Europe and Asia – is that sustainable finance is at a crucial juncture. The deadline for the UN Sustainable Development Goals is 2030. The same year also became prominent in 2019 as the tipping point for a raft of potentially catastrophic climate outcomes.

We have barely a decade to make massive social and environmental changes, many of which will require investment on an almost unprecedented scale.

Even in Europe – the acknowledged world leader in sustainable finance – the mood is increasingly concerned. Great strides have been made, but speakers at the International Capital Market Association's annual Green and Social Bond Conference in Frankfurt in June 2019 freely acknowledged that the pace of capital redirection has to accelerate rapidly to achieve carbon-reduction goals.

It was noted, for instance, that while many companies and bond issuers have adopted sustainable finance, there are still large swaths of the world economy that are not engaged with the conversation. This includes big chunks of the industrial sector – companies that may not be on the front line of carbon transition, like those from the resources or energy sectors, but which are often huge power consumers.

The equity market is making rapid steps towards understanding the materiality of environmental, social and governance (ESG) risks.

Debt is further back on the grid, but product developments point to an improved trajectory. For instance, many bankers believe the sustainability-linked loan (SLL) will be a crucial tool in taking the debt market to a new understanding of ESG on an entity, rather than an asset, basis.

The name of the game is transition. Green bonds have been a useful step towards engagement with sustainability in the debt market and most market participants believe they will continue to have a place. But the next stage is really granular understanding of the nature and scale of ESG risks borrowers face and revising the cost of capital to reflect them. In effect, sustainable finance needs to become, simply, finance.

The loan market is moving, but bonds are still lagging. There have been two sustainability-linked bonds from the same European issuer, issued in 2019, which did not contain a coupon step-down for good sustainability performance. This sector is yet to take off, for sure.

The Australian market actually is progressing quite well considering the limitations placed on it. Green, social and sustainability (GSS) bond issuance is growing, though it remains a fraction of the total and the majority of issuers are not close to bringing deals.

There is a lot of hope for SLLs, which many believe could be a game changer for volume in sustainable debt and as a source of assets off which banks can issue in GSS format.

In the background, though, looms a government that has barely progressed beyond outright climate-change denial. This policy environment makes some market ambitions impossible. How can lenders plan for energy transition when an emissions-trading scheme is treated like a disease pandemic – something to be guarded against and kept at bay at all costs?

I write these words as Australia commences what threatens to be a historically devastating bushfire season.

The federal government has cleverly triangulated its response to this natural disaster, walking the tightrope that any specific fire emergency cannot be directly linked to climate change to insist that discussion of Australia's increasingly volatile environment is somehow inappropriate.

Ironically, it is the smoke in their eyes that may make the Australian electorate see more clearly where national priorities ought to lie. Capital markets must be prepared for even heavier lifting when they do. •

“IRONICALLY, IT IS THE SMOKE IN THEIR EYES THAT MAY MAKE THE AUSTRALIAN ELECTORATE SEE MORE CLEARLY WHERE NATIONAL PRIORITIES OUGHT TO LIE.”

JEAN-JACQUES BARBÉRIS HEAD OF INSTITUTIONAL AND CORPORATE CLIENTS COVERAGE **AMUNDI**

GOING ALL THE WAY

With €1.6 trillion (US$1.7 trillion) in assets under management, **Amundi** is Europe's largest asset manager and in the top 10 worldwide by funds under management. The firm is recognised as a powerhouse in the environmental, social and governance (ESG) space and it is working toward an ambitious plan for 2021. **Jean-Jacques Barbéris**, head of institutional and corporate clients coverage at Amundi in Paris, outlines this plan and the strategies for how to achieve it.

A key theme in this yearbook is the evolution of the sustainable-debt market, from labelled green, social and sustainability (GSS) bonds to wider ESG assessment of borrowers. What is Amundi's take on this?

We are definitely seeing more investors and asset managers integrate ESG and sustainability into their investment practices. There are many reasons for this, relating to respecting certain values, integrating long-term risks, generating impact and ensuring sustainable performance.

We have shown in our research that since 2014 the integration of ESG is a source of outperformance in equities in Europe and North America.

In a sense, green bonds are an easy first step into responsible investing. The principles that govern green bonds are public, the fixed-income asset class is a familiar one and, as balance-sheet bonds, green bonds are very similar to conventional bonds.

For issuers, green bonds are an answer to a need to communicate on their ESG practices and for financing specific green segments of their overall business activities. For investors, green bonds are a useful tool to channel funds into green projects and to make it possible to measure impact.

We welcome this development because we believe that in the near future all bonds will need to be some shade of green and all finance will need to be sustainable if we are to meet the Paris Agreement goals.

Can you give some colour on Amundi's work in the ESG space?

ESG has always been an integral part of our DNA. In fact, responsible investment was defined as one of the four founding pillars of the company.

Our ESG track record and the expertise we have built up over the past decade have placed us as a key partner for many institutions when it comes to ESG investing.

Amundi has more than €300 billion in responsible-investment assets under management. We have built an unrivalled green-bond franchise, with €12 billion in green bonds under management and more than €3 billion in green-bond thematic strategies.

We also have key public-private partnerships with several leading development institutions worldwide to expand the green-bond market.

The first is with International Finance Corporation (IFC), for emerging markets. We launched the largest green-bond fund dedicated to emerging green bonds – the US$1.4 billion Amundi Planet Emerging Green One fund.

The second is with European Investment Bank (EIB), under the name Green Credit Continuum. We have set up a holistic programme to develop green high-yield bonds, green securitised credit and green private debt to finance the transition to a low-carbon economy in Europe more efficiently.

Third is the partnership with Asian Infrastructure Investment Bank (AIIB), where we are developing the first investment framework incorporating all dimensions of climate change as defined by the Paris Agreement. These are transition risk, physical risk and green opportunities.

For us, it has not been 'first green bonds, now ESG', but more 'ESG and green bonds from the start'. When we invest in a green bond we also carry out ESG analysis at the issuer level, looking at issues ranging from corporate governance and social practices to environmental activities.

For us, green bonds and ESG analysis go together.

How far has the finance sector come in the journey toward capital allocation being realigned to meet global targets like the Paris Agreement and UN Sustainable Development Goals (SDGs)?

As an industry, we still have a long way to go to ensure 100 per cent of finance is sustainable. In this vein, we have an ambitious ESG plan for 2021: 100 per cent ESG. This plan has three pillars.

The first is mainstreaming ESG investing. This means 100 per cent ESG integration in all our open-ended funds, 100 per cent coverage for our ESG analysis and systematic integration of ESG into voting decisions. The latter is key because ESG is about more than selecting ESG winners and losers. It is also about accompanying investees and fostering ESG integration in their own businesses.

The second pillar is about fostering innovation, including innovative climate solutions, much like the partnerships with IFC, EIB and AIIB. It is also about moving beyond climate and integrating the social aspect of ESG. Indeed, we believe a successful transition to low carbon must be just and fair if it is to be successful.

The third pillar is to accompany and advise investors, to share knowledge and best practices and to continue contributing to thought leadership.

Amundi has been an ESG pioneer from the start, and this continues to define our strategy today.

Looking to the future, will there continue to be a role for labelled GSS bonds even as the mainstream debt market gains better understanding and incorporation of ESG risk?

Given the rapid development of the green-bond market and the various new instruments that are sprouting – such as social, sustainability and transition bonds – we see no slowdown in this global market in the near future.

ESG investing has many different drivers; there is no one-size-fits-all. Green bonds may be an attractive solution for investors seeking more direct exposure to green activities, while other investors may have more of a broad risk approach and seek ESG integration without specific GSS bond exposure. Green bonds are also a great engagement tool for investors, to enable them to discuss green practices and green activities within issuers as well as to obtain more transparency and data on impact indicators.

This does not mean the green-bond market is static. Here I would mention three things. For one, we believe some responsible investors will become pickier in their green-bond analysis, with stricter guidelines on eligible projects, acceptable use of proceeds – for instance, limiting working capital – and reporting and transparency.

Second, if we are to finance the energy transition and bridge investment gaps effectively, we need to expand green debt markets beyond their current state of development, in which they are mainly centred on large, investment-grade issuers.

In this regard, Amundi has identified three major frontiers. There is a geographic frontier: we need to bring climate financing to emerging markets, where climate change is even more acute than in developed markets. There is an issuer frontier: channelling funds to new types of actors, in the public sphere – such as cities and local governments – and in the private sector, beyond the usual suspects, which are large utilities and energy companies. Finally, there is an instrument frontier: from developing private debt, securitised credit and other segments of the debt market. This will enable us to channel funding to individuals, small-scale projects and activities that are highly impactful.

The third aspect of evolution in the green-bond market is the growing range of labels of bonds emerging: green, social, sustainable, blue, transition and sustainability-linked, to mention a few. We believe there will be increasing need for clarity and transparency for investors and issuers.

Is the final state the existence of a niche 'dark-green' market of ethical investment alongside a mainstream that is exclusively 'light green' – ie that understands and appropriately evaluates ESG risk without having specific ethical mandates?

We are already seeing evidence of this shades-of-green approach. Cicero, for instance, has introduced a methodology to grade dark-green, medium-green and light-green.

A word of warning, though. Definitions of what is green and how green it is will probably vary from one region and one sector to the next. The key is making sure investors get more information, and of higher quality, on what they are financing, with more explicit impact reporting. This does not mean we should only finance dark-green activities. It means we need to have a better understanding of what exactly it is we are financing.

> "Definitions of what is green and how green it is will probably vary from one region and one sector to the next. The key is making sure investors get more information, and of higher quality, on what they are financing, with more explicit impact reporting."

One of the main developments in the GSS bond market in 2019 was the delivery of the EU taxonomy. What does this mean for a large, sophisticated investor like Amundi? Is Amundi using the taxonomy as a basis for reporting or as a performance benchmark for its investments?

The taxonomy will be a useful tool for responsible investors like Amundi. Indeed, one of the main challenges of the GSS bond market is to translate climate-change policies and objectives into actual investments and ensure the projects financed have a real, positive and transparent environmental impact.

The taxonomy will bring much-needed clarity on what we can consider green and what we cannot. As such, it should generate interesting discussions on the types of impact-reporting indicators we should seek out from issuers when financing their green projects.

It is important for us that this taxonomy is enacted in a an environment that seeks to support and accelerate sustainable finance, including the elaboration of the EU's own green bond principles, the Green New Deal of the European Commission (EC), so as to stoke public investment and also regulation – especially in the crucial field of carbon pricing.

The taxonomy is not finalised yet so we don't have complete visibility on what its final output will be. However, we have started to implement its philosophy, notably in the Green Credit Continuum programme which we launched in partnership with EIB. It is a direct answer to the Green New Deal of the EC: channelling financing to segments of the green-bond market that are still underdeveloped – high-yield bonds, private debt and securitised credit. All investments will need to contribute in one way or another to the EU's environmental objectives.

We are also using our own ESG tools and in-house green-bond analysis.

We have seen ESG investors developing their own taxonomies and guidelines (see p26). How does Amundi assess the ESG performance of its investments outside the labelled GSS universe – where second-party verification and impact reporting are par for the course?

Over the past decade, Amundi has developed a strong responsible investment set-up with large resources dedicated to providing in-house assessments of our investments.

We have a proprietary ESG analysis and rating methodology. In stylised terms, the methodology can be broken down into three steps. First, we define a set of criteria per sector for each of the E, S and G pillars. We weigh these criteria based on each sector and assess the quality of data providers for each.

We then combine these criteria as well as weights and inputs from data providers to compute an ESG score, which is updated monthly and is followed by ESG analysts.

Third, we hold regular meetings with the companies, industry experts and relevant stakeholders – such as NGOs – to provide qualitative input to the ESG score.

We currently cover more than 8,000 issuers as well as the main equity and fixed-income indices. Our ambition is to increase this coverage extensively.

We also implement an engagement policy to foster better ESG practices, through ongoing engagement, voting and dialogue. In 2018, we voted in nearly 3,000 AGMs.

Finally, we take part in numerous collective initiatives, such as the UN Principles for Responsible Investment, Climate Bonds Initiative, the Green Bond Principles, the Task Force on Climate-related Financial Disclosures and the One Planet Sovereign Wealth Fund Working Group.

What types of ESG reporting does Amundi provide to its clients?

Amundi provides reporting on ESG that is standard and tailor-made, which can cover portfolio and benchmark scoring, ESG rating coverage and definitions of ESG criteria. We can also provide investors information on specific needs, such as carbon- and green-bond impact reports – including data such as avoided emissions per million dollars invested per year and breakdown of avoided emissions per bond.

Climate risk is now more proximate than ever. Should bond investors be confronting the reality of material climate impact on investments in the lifetime of current exposures? Where are the main risks – by sector or jurisdiction?

There is a definite need to integrate climate risks into portfolios, including bond portfolios. In fact, there is a need to integrate all dimensions of the Paris Agreement to be more resilient.

The first is physical risk – focusing on issuers and activities aligned with climate-change adaptation efforts. Then there is transition risk, when we talk of regulation, changing consumer habits and so on, which focuses on issuers and activities aligned with climate-change mitigation. Finally comes green opportunities – supporting innovative actors making headway in low-carbon activities.

With AIIB, we are devising the first investment framework that incorporates all three dimensions. It defines three types of issuers: those that perform poorly on these dimensions are excluded, those that are moving in the right direction are eligible and targeted for engagement, while those that outperform for all variables are also eligible.

By targeting these issuers, our investment strategy becomes more resilient to climate-change-related risks but also more exposed to opportunities not necessarily priced in the market.

"There is a definite need to integrate climate risks into portfolios, including bond portfolios. In fact, there is a need to integrate all dimensions of the Paris Agreement to be more resilient."

What is the next phase of evolution for sustainable debt globally? What should we look for in 2020?

We would like the market to develop around standards that are clear and simple and that foster greater transparency. Issuers should improve their way of communicating on their ESG policies as ESG ratings will inevitably become as important as, or an integral part, of credit ratings. Also, as social issues become more important, we would like to see more social bonds. •

Green Bond Principles adapt as market innovates

The world's first sustainability-linked bond and the evolution of transition bonds have led the executive committee of the Green Bond Principles (GBP), with the support of the International Capital Market Association (ICMA), to agree to embrace a wider scope of bond products for a more sustainable, low-carbon economy.

BY SAMANTHA SWISS

The GBP and ICMA are embracing change brought into the sustainable bond markets during 2019.

Two innovations in particular mark a step away from assessments based on the assets underlying a bond towards analysis of issuers' overarching sustainable strategies, policies and objectives. However, while the new products have this in common, they are structurally different.

The first – transition bonds – is a use-of-proceeds instrument akin to traditional green bonds. The second – sustainability-linked bonds – is a target-linked instrument similar to sustainability-linked loans (SLLs).

The emergence of these products has resulted in much discussion and debate among bond-market participants. By and large, they view market experimentation with new products as a positive step in the ongoing evolution of sustainable finance in the bond world.

It is clear, however, that to achieve the credibility and rigour now apparent in the more established products – green, social and sustainability (GSS) bonds – work needs to be done to set market-based guidelines and principles for the new instruments.

While the innovations have come via transactions, it makes sense that a broad-based market initiative like the GBP – including the related Social Bond Principles and Sustainability Bond Guidelines – which already provide a de facto global standard for the GSS market, takes the lead in analysing the new products and gaining consensus on appropriate structures.

TRANSITION BONDS EVOLVE

The first big innovation in the sustainable-bond markets in 2019 was the further development of transition bonds. The idea is to support companies shifting to less carbon-intensive business models.

There have been various initiatives on transition bonds over recent years, most occuring in 2019. These include issuance from the corporate sector, a global investor setting guidelines for the products and the first issuance of these instruments in the supranational, sovereign and agency sector.

Corporates took the lead. The first recorded transition bond was issued in July 2017 by Hong Kong power producer Castle Peak Power Company, a subsidiary of CLP Holdings.

FOUR CORE COMPONENTS OF THE GBP

The June 2018 edition of the International Capital Market Association's Green Bond Principles (GBP) reiterates the initiative's four key components. These are:

1. Use of proceeds of the bond for green projects.

2. Process for project evaluation and selection.
The issuer should clearly communicate to investors:

- The environmental sustainability objectives.
- The process by which the issuer determines how the projects fit within the green projects categories identified for the use of proceeds.
- The related eligibility criteria applied to identify and manage potentially material environmental and social risks associated with the projects.

3. Management of proceeds. The net proceeds of the green bond, or an amount equal to these net proceeds, should be tracked by the issuer in an appropriate manner and attested to by the issuer in a formal internal process linked to the issuer's lending and investment operations for green projects.

4. Reporting. The issuer should make, and keep, readily available up-to-date information on the use of proceeds, to be renewed annually until full allocation, and on a timely basis in case of material developments.

FEATURE

THE ICMA VIEW

The Green Bond Principles (GBP), as well as the related Social Bond Principles (SBP) and Sustainability Bond Guidelines (SBG), are key initiatives of the International Capital Market Association (ICMA). Nicholas Pfaff, senior director, market practice and regulatory policy at ICMA in Paris, is the secretary to the GBP. He talks exclusively to *KangaNews* about ICMA's role.

What are the operating dynamics between ICMA and the GBP?

The GBP, as well as the SBP and SBG, are part of ICMA but also have their own governance and an executive committee.

ICMA convenes, supports and advises for the GBP. We do everything we can with the skillset we have to help bring forward the best practice agreed upon, using our in-depth knowledge of capital markets and our understanding of what is happening in the regulatory community.

But it's not ICMA that's cooking up the GBP, SBP and SBG. This is a global, wide-based and objectively impressive market initiative. When we have discussions at ICMA about its success, we of course take some credit for it. But this is a broad and international market initiative – with global investors, issuers and underwriters coming together in an unprecedented way on a topic of incredible importance.

What is ICMA's role when it comes to market innovation – such as around transition and sustainability-linked bonds?

There is a fine balance between not anticipating the market – so we have to build on what the market does and experiments with – and not finding ourselves on the back foot when the market starts developing rapidly and there are issues that require the market to reflect on best practice and dealing with potential problems.

This is where the GBP is in an extraordinary position. It is arguably one of the most active, large, international and structured market initiatives with which we have been involved.

As the sustainability theme expands and becomes more mainstream, we think the GBP is the natural forum to have this discussion and contribute to best practice. At the same time, the GBP can expand its own brief beyond use-of-proceeds green, social and sustainability (GSS) bonds.

There has been quite a lot of debate over the last year around whether too many labels are being created in the thematic-bond space. Has ICMA decided on any policy or course of action with regard to labelling?

It is inevitable that there will be experimentation around labels as the sustainable bond market evolves. However, we want to avoid the proliferation of labels because this can lead to confusion.

For best practice and clarity for investors and regulators, it's better that we be rigorous about these things. This means sticking to a labelling nomenclature that is well understood and with which market participants are reasonably consistent.

How much clout does ICMA have when it expresses a view like the one on labelling?

We are not a regulator. We focus on best practices and we depend on consensus and the collective legitimacy of the market participants with whom we work. However, I would say it's generally quite powerful when ICMA says something is best practice. The market pays attention, as it should.

Nevertheless, the market will legitimately experiment and may label a transaction differently. If it comes back to ICMA and the GBP executive committee, we can express our common view. We have to remain steady in our role of arbitrator and promoter of best market practice.

There are concrete examples of regulators taking our views into account. For example, there's now a debate about a regional green-bond standard in Europe. I represent ICMA and the GBP executive committee as a member of the EU Technical Expert Group on Sustainable Finance (TEG), so we have been at the core of the debate around this.

At the beginning, the EU Commission considered whether it needed to start from scratch. However, as the GBP is the result of a transparent process and has great market legitimacy, the commission focused on identifying issues as opposed to starting from zero.

The recommendations of the TEG are explicitly based on what the market has done and refer specifically to ICMA and the GBP. This is a real endorsement of what we have been trying to do in this space. It's a measure of our success when regulators and supervisory bodies de facto endorse what the market has developed with ICMA's support.

"As the sustainability theme expands and becomes more mainstream, we think the GBP is the natural forum to have this discussion and contribute to best practice. At the same time, it can expand its own brief beyond the use-of-proceeds green, social and sustainability bonds."

NICHOLAS PFAFF INTERNATIONAL CAPITAL MARKET ASSOCIATION

The US$500 million 10-year energy bond was issued to pay for a natural gas plant the company says is critical to Hong Kong's efforts to cut carbon emissions.

CLP Holdings' Climate Action Finance Framework states that the company's climate-action bonds – which include energy-transition or emission-reduction bonds – align with the GBP.

In February 2019, Italian natural gas infrastructure company Snam issued a €500 million (US$553 million) August 2025 climate-action transition bond. Proceeds will fund the company's investments in biomethane and energy efficiency, along with those aimed at reducing its methane emissions by 25 per cent by 2025. A second-party opinion on the Snam bond, provided by DNV GL, states that it is aligned with the GBP.

Six months later, Brazilian cattle producer Marfrig Global Foods (Marfrig), issued a US$500 million 10-year sustainable transition bond. Proceeds will be used to buy beef from cattle farmers in the Amazon Biome that avoids land in areas the Brazilian Institute of the Environment has embargoed, such as deforested areas or where land use would threaten indigenous rights. Vigeo Eiris's second-party opinion on the Marfrig bond states that it is aligned with the four core components of the GBP and SBP voluntary guidelines issued in June 2018 (see box on p21).

Until 2019, there were no set definitions or parameters for transition bonds. AXA Investment Managers (AXA IM) took up the challenge and published draft guidelines in June (see p26). Its goal was to facilitate broader deployment of sustainability principles in the bond market.

Explaining the rationale for transition bonds, Yo Takatsuki, head of environmental, social and governance (ESG) research at AXA IM in London, said: "We are calling for the establishment of a new type of bond, distinct from green bonds. While green bonds are intended for issuers to use the proceeds to finance environmentally friendly projects, we see a significant gap where investors could deliver real impact for companies not yet at this stage. There is an opportunity to provide finance to companies that are brown today but have the ambition to transition to green."

Crédit Agricole issued the first transition bond under AXA IM's guidelines at the end of November 2019 – a 10-year €100 million private placement, of which AXA IM was the sole purchaser. The bank will earmark an amount equivalent to the proceeds of the bond for loans made to projects in carbon-intensive sectors that will contribute to the transition to a low-carbon economy. Takatsuki confirms the bond is aligned with the core components of the GBP.

In a further evolutionary step, in October 2019, European Bank for Reconstruction and Development (EBRD) issued its first green-transition bond. The proceeds of the €500 million five-year bond are earmarked for supporting EBRD's green transition project portfolio. This comprises investments in energy and resource efficiency, including the circular economy and sustainable infrastructure such as low-carbon transport and green logistics.

In its green-transition-bond template, EBRD states: "The carbon intensity and environmental vulnerability of EBRD's region [make] it especially exposed to climate-related risks… To address this challenge, EBRD recognises that there is an urgent need for projects to go beyond supporting assets that are considered already to be low carbon…to finance investments in those sectors of the economy that today are highly dependent on the use of fossil fuels, thereby enabling them to transition to low-carbon and resource-efficient operations."

EBRD's green-transition bonds also align with the four core components of the GBP. In an opinion piece published in *Environmental Finance* in November 2019, Isabelle Laurent, EBRD deputy treasurer and head of funding, and Carel Cronenberg, associate director, head of monitoring, reporting and verification, energy efficiency and climate change, state: "Green transition projects should not be considered 'light green' projects, and do not, in our view, need any derogation from all core components of the GBP."

They add: "Indeed, our *ex-ante* assessment of the CO_2e savings of our portfolio of projects underpinning our green transition bonds is approximately 2.75 times greater than those associated with our environmental sustainability bonds for each euro or dollar invested."

NEW GROUND FOR SUSTAINABLE BONDS

The second – and more controversial – innovation in 2019 was a type of bond that mimics the SLL product, which has shown impressive volume growth in its relatively short history.

In September 2019, Italian energy company Enel issued the first sustainability-linked bond. The US$1.5 billion five-year transaction offers a 2.65 per cent coupon that will increase by 25 basis points if Enel does not achieve, by 31 December 2021, renewable generation capacity that is at least 55 per cent of its consolidated installed total.

The same company issued a second sustainability-linked bond in October. The €2.5 billion three-tranche deal has a similar structure to the earlier US dollar transaction. The €1 billion June 2024 tranche and the €1 billion October 2034 tranche both have a 25-basis-point coupon step-up on the same terms as the US dollar deal. Meanwhile, the €500 million October 2034 tranche offers an interest rate that will increase by 25 basis points if the company fails to reduce greenhouse-gas emissions to no more than 125 grams of CO_2 per kilowatt-hour by 2030.

These transactions echo the €200 million ESG-linked *Schuldschein* issued by German engineering group Dürr in June 2019. The coupon on this product can increase or decrease according to the company's sustainability rating. A *Schuldschein* is a German private debt instrument that shares aspects of loans and bonds – it has been described as a loan in the form of a bond.

Enel's sustainability-linked bonds do not align with the four core components of the GBP. There is no requirement for specific use of proceeds, the focus instead being on the issuer's strategy to transition to a low-carbon economy. There is also no requirement for a green-bond framework or for second-party opinion reports, nor for any reporting on the assets during the life of the bond.

These target-linked instruments have created a flurry of debate. *Environmental Finance* has reported that at least one big green-bond investor called the deals "greenwashing" because the company is doing no more than offering an option on not

> "We need to say to companies it's okay if you come from the brown sector as long as you are moving in the right direction, you have a clear strategy for transition and you are playing with open cards when you issue transition bonds."
>
> **LARS EIBEHOLM** NORDIC INVESTMENT BANK AND GREEN BOND PRINCIPLES EXECUTIVE COMMITTEE

delivering its renewables goals. Other investors and underwriters have lauded the development. Benefits cited include helping bondholders advance UN Sustainable Development Goals (SDG)-related targets, enabling greater volume of sustainability issuance by moving beyond eligible use of proceeds and allowing a stronger focus on strategic alignment with global goals at the corporate level due to the emphasis on ESG integration.

BEST PRACTICE

In a sector evolving at such a furious pace, a key issue is how new products can offer the same degree of rigour, transparency and credibility that has been established for more traditional GSS bonds via the GBP, SBP and SBG.

The GBP executive committee and ICMA have been discussing the role of the principles in this context (see box on p22). Lars Eibeholm, treasurer at Nordic Investment Bank in Helsinki and chair of the GBP executive committee, tells *KangaNews*: "It has become clear that we need to discuss what we are facilitating. Is it only GSS bonds or do we have a bigger agenda?"

This has led to what Eibeholm calls "vision and mission" discussions within the executive committee. He confirms that a wider mandate is on the cards. "We have decided that the GBP can look into a wider scope of bond instruments that can facilitate a move to a more sustainable and low-carbon economy where bond-market financing can be used."

As such, the committee has been deep-diving into the details of transition and sustainability-linked bonds.

TRANSITION PROGRESS

By January 2020, of the new asset classes the GBP had made most progress on transition bonds. Following the establishment of a taskforce, a Climate Transition Finance working group was established in November 2019. Coordinated by AXA IM, HSBC and J.P. Morgan Chase, the working group's terms of reference state that it will consider the concept of transition financing in the context of the green-bond market.

The terms of reference state that the working group will not retrospectively reassess and validate the credibility of self-labelled transition bonds already issued. Instead, it "is purely focused on understanding why corporate issuers from carbon-intensive industries have been largely absent from the green-bond market thus far and considering providing guidance for potential future issuance".

There are two key areas of focus for the working group, according to the terms of reference. First is industry diversification. The aim is to assess why issuers from across bond market segments have been largely absent from the green-bond market despite their importance to climate transition.

Second is the importance of issuers' climate strategy and financing. This will entail reviewing the application to issuers absent from the green bond market of GBP Pillar 2 – process for project evaluation and selection.

No doubt there will be much to report on during the year ahead as the working group gets into action. However, Eibeholm confirms that a transition bond issued under the AXA guidelines and EBRD's climate transition bonds are covered by the GBP, as both follow the four core components of the principles.

Eibeholm agrees that companies in transition need to be encouraged to raise funding. "We all realise that aiming for a 1.5-degree target demands a huge effort," he says. "The way our economy operates needs to completely transition, while still aiming for GDP growth. We need to encourage not just the companies that already fulfil the requirements for a sustainable economy but all the others, too."

It will be important, however, to set the right criteria for transition bonds. This is where the GBP executive committee believes it can play a key role. "We need to say to companies it's okay if you come from the brown sector as long as you are moving in the right direction, you have a clear strategy for transition and you are playing with open cards when you issue transition bonds," Eibeholm explains.

He adds that if issuers do this, the GBP – backed by its issuer, underwriter and investor members – will be accommodating and accepting of transition-bond issuance.

According to Eibeholm, one of the advantages of the involvement of the GBP, SBP and SGB in the bond market is that this mitigates the risk some issuers face of their bonds not meeting key players' green standards. He comments: "Many issuers are wary of issuing a bond that follows the GBP but is then not viewed as such by the market, a stock exchange or industry body. We need to mitigate this risk and have clear guidance for a wider scope of issuance as long as the bonds meet certain standards and promote integrity. This comfort is needed to propel the market forward."

When it comes to labelling different types of products, Eibeholm says bonds – whether they be green, blue, social, sustainability, SDG, transition or any other labelled bonds – are all strategies that follow the four core components of the GBP. He explains: "Underpinning the labels are strategies. The labels point to the impact or objectives an issuer wants to achieve."

Once an issuer has set its strategy, Eibeholm says, it can choose between two kinds of instruments. These are use-of-proceeds bonds – like green or transition bonds – and general corporate-purpose bonds with KPIs linked to the issuer's sustainability performance.

Sustainability-linked bonds do not follow the core components of the GBP, Eibeholm says. Nevertheless, linking back to the vision and mission discussions at the GBP, the executive committee thinks it is valid to consider sustainability-linked bonds.

As Eibeholm comments: "This is where the 'vision and mission' discussion is important. We could have said sustainability-linked bonds are not for the principles to consider because we focus only on use-of-proceeds bonds. But the group decided we needed to have a larger and much broader outreach because our purpose is to facilitate the transition to a low-carbon economy, not just the instruments using green, social, sustainability and other labels."

As a result, the GBP executive committee has set up a taskforce to look into sustainability-linked transactions. In early January 2020, Eibeholm told *KangaNews* the taskforce would be evolving into a working group for sustainability-linked bond products. "We hope to make an announcement by mid-January. As soon as this is done, we will publish the terms of reference for the working group." •

OPENING *TRANSITION PATHWAYS*

KangaNews talks to **Yo Takatsuki**, head of ESG research at **AXA Investment Managers** (AXA IM) in London, about the ground-breaking guidelines for transition bonds his firm published in June 2019. Takatsuki was instrumental in formulating the guidelines. He shares his insights into the urgency of opening up the transition pathway so carbon-intensive industries are encouraged to work towards aligning with the Paris Agreement.

Why does AXA IM think transition bonds are important?

The first and foremost consideration we have as a large provider of capital to industry, governments and markets generally is the role we can play in achieving the Paris Agreement goals.

Over the last few years, we have been directing capital away from some areas – such as coal and power plants – and investing it into green assets. We have done this on behalf of our parent insurance entity, AXA Group, as well as third-party clients including Australian super funds.

We think this will continue and it's important as a strong signal we can send to the market. For example, we currently have around €5.5 billion (US$6.1 billion) invested in green bonds. The credibility and robustness of green bonds is important. However, we cannot get away from the fact that 10 years into this market, although it has grown a lot, it has largely been limited to supranational, sovereign and agency (SSA) issuers, commercial banks and electricity utilities in Europe and North America.

What we haven't seen in the green-bond market is what I would call the bulk of the real-world economy. The 20th-century post-war economy has been built on heavy industry and manufacturing. When we talk about the challenge of achieving the Paris Agreement goals, it's these areas that we need to transition. They include carbon-intensive industries such as chemicals, manufacturing, cement, real estate, and car transport, as well as the extractives companies themselves, which provide the supply side.

We felt something needed to be provoked, to change, to ensure that these companies could be encouraged and motivated to go down the path of meeting the Paris Agreement goals. This is what is called the transition pathway. One of the tools we think will help in the fixed-income space is transition bonds.

It's interesting that it was an asset manager that came up with the guidelines.

We felt that with transition bonds, investment banks would be conflicted in trying to publish guidelines, while a single issuer never carries the breadth of the market as issuers can be quite narrow in their views. A not-for-profit or second-party opinion provider doesn't carry the weight necessary to publish guidelines.

There are really only two groups that could feasibly and credibly publish guidelines. One is regulatory bodies such as the Bank of England. But it's unlikely they would want to be prescriptive about exactly how it's done. The other is a large global asset manager like AXA IM, which is a holder of securities in the entire global economy.

We felt it was our responsibility to add to the debate in moving forward the push to corporate decarbonisation.

Another option would have been a body like the International Capital Market Association (ICMA), which has already published green and social bond principles as well as sustainability-bond guidelines.

AXA IM sits on the ICMA Green Bond Principles (GBP) executive committee, which is composed of eight investors, eight green advisory investment banks and eight green-bond issuers. Together, we have made a commitment to oversee and guide the future of the market.

AXA IM published the guidelines not as the final picture but as a way to provoke discussion. We know for such a thing to become a market reality we need a broad cohort of participants to agree on the common language and guidelines that will be the basis for issuers to come to market with transition bonds.

I've spent a lot of time the last four months working with ICMA. A working group has been set up, called the Climate Transition Finance Working Group. AXA IM is a co-chair, alongside HSBC and J.P. Morgan. Terms of reference for transition bonds have been published on the ICMA GBP website.

We are now working out who will participate in the group – I've had more than 50 applications from a wide range of stakeholders. You can tell this is a big area of interest.

At the ICMA annual conference in June 2019, the idea was raised that with so many types of thematic bonds,

the market may be becoming too complex. Do we really need another label for transition bonds or are they just another form of green bond?
The issue of having one more label is very low down the pecking order in my considerations. We already operate in a complicated and jargon-ridden financial market. What we need to be thinking about are the ways in which we can achieve the greater end.

We believe transition bonds are a way to do this. Others may disagree. But to me this is not an issue of simply asking whether we need another label. If others don't want to have labels, they are welcome to participate in the ICMA working group and make their point. The working group is there for this – to make sure there are no unilateral decisions.

How do you measure transition?
This is an area where there has been a lot of debate thus far. My view is that elsewhere, and then work out how this applies within the context of fixed income, firstly, and then within the context of use-of-proceeds bonds. There will be a lot of scrutiny of issuers' practices around climate strategy and climate performance.

There seems to be another kind of transition happening – from use-of-proceeds product to looking at issuers' overall sustainability performance. From what you're saying, a transition bond crosses both these concepts – it involves use of proceeds but there's also an assessment at the issuer level.
That's right. The green bond is quite an ingenius structure in that one of its achievements has been significantly to improve investors' expectations around transparency and commitment from a bond issuer. There's an accountability element to these bonds that didn't exist in the fixed-income market before.

10 dollars. You would probably say this sounds reasonable, as it would be good for my health. This is like a green bond.

For transition bonds, there's a slightly different nuance. Imagine I said to you I'm really unfit so I'm going to run one kilometre a week, can you give me 10 dollars each time I run? You would probably say you didn't think that was sufficient. But what if I said in three years' time I would be running a marathon and in two years' time I'll run a half-marathon? It's just that today, because I've done no exercise for many years, I can do only one kilometre. You might then be inclined to sponsor me.

What counts in the story of transition is the long-term ambition to decarbonisation, with interim targets in place to contextualise the progress. As a result, the issuer-level information that gives context and colour, meaning, direction and commitment to the specific activities being financed is increasingly important.

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our role is not to define transition. There are already credible, science-based institutions out there – like the Science-Based Targets Initiative and the Transition Pathway Initiative. There is also the work the Institutional Investors Group on Climate Change (IIGCC) has done around Climate Action 100+. All these have looked at the concept of climate transition for carbon-intensive industries.

One of the important tasks of the ICMA working group is to make sure the other bodies' work and input is reflected in what we do.

We will take expert knowledge, developed, refined and resourced

The use-of-proceeds tool is focused on specific issuance. The broader activities of a corporation will not necessarily hinder investment in the bond. Although some investors – AXA IM included – do quite a lot of issuer-level homework on the green bonds they buy, in general nothing is stopping the world's most polluting company with a large green-assets base from issuing a green bond.

I describe the nuanced difference between green and transition bonds as follows. Say I said to you I'm not fit and I really need to do some exercise so I'll run five kilometres a week. Then I asked that every time I did this, you gave me

The good thing is that considerably important developments have happened in the last couple of years to facilitate this. One example is the establishment and rollout of the Task Force for Climate-related Financial Disclosures (TCFD). With this, we have specific language and a framework for thinking about climate disclosure. There are now expectations around governance and understanding the risks to a business. Companies are already grappling with these issues and investors are increasingly wanting to see this happen.

A lot of the work of Climate Action 100+ is trying to get companies to commit to and publicly support the TCFD framework so they start reporting against it.

We want to make sure the work we are doing in this pocket of the fixed-income market is consistent with the broader objectives investors have in trying to help achieve the Paris Agreement goals.

Like the GBP, AXA IM guidelines on transition bonds have four core components – use of proceeds, process for project evaluation and selection, management of proceeds and reporting. Transparency and disclosure are obviously key elements. ICMA has analysed transparency and disclosure for green and social bonds. How will these be assessed and verified for transition bonds?
One of the conversations I've been having with companies and investment banks is around the iteration that is likely to happen in the transition-bond market. If you look back at the evolution of green bonds, for example, the early bonds were nothing like the products we are seeing in the market today.

The same thing needs to happen with transition bonds – it will be an iterative process to get all the elements in place. The answer cannot just be AXA IM saying what a transition bond is, how to measure transition and what transparency and disclosure are required. At some point, we will start to have large, public issuance of what we consider to be transition bonds – and other market participants might take a different view.

Through this natural, iterative process of the market's response, the concept of transition bonds will be refined. No amount of theorising and writing down on paper will be a replacement for the market actually happening.

In this context, you must be delighted with the Crédit Agricole transition bond issued on 27 November. The 10-year €100 million (US$111 million) bond was issued as a private placement subscribed by AXA IM and is the first bond to be issued under the AXA IM transition-bond guidelines.
Yes. We have been working with Crédit Agricole since the summer. Our idea was to work on a private placement that would be a proof of concept for transition bonds. We approached Crédit Agricole because it is a leading bank in the green-bond space and we have a high level of respect for the bank, we value its expertise in this market.

Why did you choose a bank that already issues green bonds rather than a company that is transitioning from brown to green?
We are having these conversations with corporates. But sometimes it takes a bit of time for issuers to get their internal work in place to be able to issue labelled bonds. In this test-case scenario, we were working to a tight timeline.

When we spoke to a handful of corporates about this, some didn't have funding needs, others wanted to wait and see how the market develops and still others said they were supportive of the idea but the challenge was meeting the deadline.

Now that we are not time-limited, we are talking to a lot of issuers and investment banks to encourage them to look into issuing transition bonds. I'm hoping we will start to see more of these deals in 2020.

What were the main challenges and lessons from working with Crédit Agricole on the transition bond?
Those that come into the market early are pioneers. They will benefit from the pioneering spirit but on the other hand there will be more scrutiny on these deals. I would say issuers' internal narrative about climate alignment and what it means to help achieve the Paris Agreement goals has to be resolved before they look at this type of product.

> "Those that come into the market early are pioneers. They will benefit from the pioneering spirit but on the other hand there will be more scrutiny on these deals. Issuers' internal narrative about climate alignment and what it means to help achieve the Paris Agreement goals has to be resolved before they look at this type of product."

If an issuer wants to come to market we are here to support and partner with them in the journey to transition. We believe this is the most important way for all of us as a society to reduce the temperature we're headed for – we want to keep it to an increase of no more than 1.5 degrees. But first, every individual corporate issuer needs to set its narrative around climate change.

In other words, a company-wide focus on climate change can no longer be just a nice-to-have.
Yes. This is not an issue of specific deals. They are only the small detail. What we want is a mindset change. That's the paradigm shift governments, corporations and investors are going through.

I would add that there's a genuine need for urgency so we can't park this paradigm shift. We all have to challenge one another in a positive, constructive way to do this together. •

THE ROUTE ***TO THE FUTURE***

As part of a rare and brief visit to Australia in December 2019, **Marilyn Ceci**, managing director and head of green bonds at **J.P. Morgan** in New York, met with *KangaNews*. Ceci does not predict that use-of-proceeds sustainable bonds will give way to general-corporate-purposes issuance with an environmental, social and governance (ESG) overlay. She views the urgency of the low-carbon-economy transition to be such that all well-considered, meaningful and deliberate steps on the sustainability path are critical.

What is your view on the concept of transition bonds? Do you think they are an important step in the evolution of the sustainable bond market?

The transition to a low-carbon economy requires a multifaceted approach. If we just issue green bonds for wind farms, we are not taking into account the overall transition the economy needs to keep global warming to 1.5 degrees by 2030 based off pre-industrial levels.

I am certainly in favour of transition bonds as one of the co-authors of the Green Bond Principles (GBP), as administered by the International Capital Market Association (ICMA). We initially focused on creating voluntary process guidelines, or best-practice guidelines, to provide flexibility to a variety of issuers to enable them to communicate their sustainability narratives.

As the green-bond market has evolved over the years, carbon-intensive industries have largely avoided getting involved – maybe out of fear of reputational risk. One naturally wants a positive outcome.

The few we have seen come to market have not really been welcomed by the press or by some investors. Thus you can understand why there is an interest in providing a different label for bonds issued in carbon-intensive industries, so that no company is calling itself something the broader market – and in many cases the press – doesn't necessarily agree with.

Are investors largely coming along for the ride around transition bonds?

Yes. In June 2019, AXA Investment Managers (AXA IM) published transition-bond guidelines (see p26). European Bank for Reconstruction and Development (EBRD) has also done some impressive work on this, and EBRD recently issued a transition bond (see p23).

We must also understand and appreciate that investors are not one homogenous group – some have differing views. AXA IM has made its view public and clear. One of the things the GBP executive committee is working on is the recently created Climate Transition Finance Working Group (see p24).

The working group will look at some of the barriers to entry to the green-bond market for some issuers, and whether it makes sense to create guidelines on best practice to help issuers with their transition narrative.

How can the market ensure credibility for transition bonds?

Guidelines are helpful. If you think about what we have done with the GBP, I think issuance really picked up in January 2014. Guidelines provide comfort and when one is in alignment with guidelines, the risks associated with claims go down.

We have made some changes to the GBP over the years, such as the enhancement of principle two – which is the process for evaluation and selection. We ask issuers to communicate very clearly how the eligible categories for their green bonds fit into their overall climate or green strategies.

Market users are quite excited about the prospect of transition bonds for a carbon-intensive economy like Australia. What do you think needs to happen for this concept to gain traction?

Australia is not the only carbon-intensive economy on the transition path. I like to think about climate change as a type of ladder. We have to appreciate that every step up the ladder is important and that different countries are on different rungs. This is one of the reasons I think the GBPs have been as successful as they have.

Transitioning to natural gas from coal, which doesn't quite meet the full objective of transitioning to a low-carbon economy, can save tonnes of CO_2 each year and can be very meaningful. To go directly to renewables from coal may not be a viable option for all.

Transition bonds will provide an opportunity to create a pathway for industries to participate meaningfully – and I think this is the important point. Some Canadian carbon-intensive industries have been circling around the transition bond for a very long time, and there has been general concern from an institutional standpoint about jumping into this space before it is fully vetted.

I cannot say this will be the outcome of the working group – it has only just begun. First, we will discuss and evaluate transition bonds with issuers, investors and underwriters. However, once the working group has had the chance to put the work in, I'm sure we will take this concept to the new Advisory Council, an addition to the GBP in 2019, and ask for further input from other stakeholders – which include both members and observers of the GBP.

One argument against encouraging the development of transition bonds is the idea that there are too many labels in the sustainable-bond market. At the ICMA annual conference in Frankfurt in 2019, there was a call for simplicity. How important are labels, and what are their disadvantages?

The idea around labels is helpful, not confusing. The idea of the label is to support transparency and disclosure.

I personally don't have a concern with labelled bonds. We have blue bonds which, to me, are a subset of green bonds. If an issuer wants to provide an additional label, who are we to say they cannot use it?

It is extremely important for issuers to make clear they are labelling their bonds as linked to sustainability considerations, and that this is why they are going to follow the guidelines they select. Investors are smart and make their own decisions regarding complexity. It is when you put a label on something and don't clarify it that problems can occur. But this is true for anything.

It is also fair to say the market will continue to evolve over time, from United Nations Sustainable Development Goal (SDG)-linked bonds, sustainability-linked revolving loan facilities and green loans to sustainability bonds, transition bonds and other types of issuance and labels.

Looking at sustainable-bond-market transition, do you agree with the idea that the market is evolving from the focus on use-of-proceeds bonds towards the concept of integrated whole-of business ESG analysis? It seems that investors are moving in this direction, while rating agencies are also starting to integrate ESG risk assessment into credit ratings (see p43).

Starting with the financial rating agencies, we have seen that they are all gearing up to make the most of this opportunity. They have extensive teams and a broad capital base to support expansion into the ESG ratings space. I understand why they view this as an opportunity.

However, it is also worth bearing in mind that if there is a material ESG risk it will already be included in a financial rating. It is important to remember that rating agencies have always included material ESG risks in their regular ratings and, in this regard, nothing has changed.

The implementation of ESG factors is becoming broader and more integrated across many investors. Obviously, this has been led by Europe, but many key US investors, such as BlackRock and TIAA CREF, have been investing in green-bond-type assets since before labels were invented.

The broad approach to mainstreaming has happened more quickly in Europe, led largely by insurance companies and pension funds that have been pushing for this – and of course asset managers that want to manage those funds' money. It is moving mainstream more quickly in the US as well of late. It is broadening out, whereas it used to be pocketed.

Historically, some asset owners feared giving up returns by taking ESG into the investment process. However, ESG integration strategies have evolved over time and the conversion process also continues to evolve. In fact, increasingly, the attitudes of many investors have changed to think that high ESG ratings for companies are an indication of forward-thinking management and can be associated with potential outperformance.

We like to encourage issuers to communicate how eligible project categories feed into their sustainability narratives and commitments. We have also seen other broad commitments to sustainability, not just the ESG score – through SDG-linked bonds for general corporate purposes or a coupon step-up if issuers don't meet objectives. This exciting development is complementary to the green-bond market.

The *Global Sustainable Investment Review*, which is published every other year and aggregates global investment, consistently mentions the growth of investors that take ESG considerations into their processes. The latest measure is US$30.7 trillion globally.

"It is extremely important for issuers to make clear they are labelling their bonds as linked to sustainability considerations, and that this is why they are going to follow the guidelines they select. Investors are smart and make their own decisions regarding complexity."


J.P.Morgan
Advancing Sustainability Through Green Bonds
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We leverage our leadership position and expertise in global debt capital markets to be a market-leading green bond underwriter.
We are committed to working with our clients to capitalise on opportunities that address sustainability challenges, using our financial resources, insights, expertise, relationships and scale.
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Green bonds provided for the market, at its inception, the concept of positive as opposed to negative screening. The green, social and sustainability (GSS) bond market is up 50 per cent compared with 2018, which is pretty impressive. The sustainability bond label, which is used for green and social projects, is growing and is up 234 per cent in 2019. Third-party certified procurement or sustainable sourcing is both green and social, so use of the sustainability bond label is a better fit. I expect significant growth in sustainability bonds in 2020.

It sounds like you don't believe there will be transition from themed bonds to ESG integration.

The growth of both is relevant and important. I don't think they are the same, but they have a tremendous number of links. I don't think the green-bond market is ending. Many asset managers have been building franchises around these instruments and they are very invested in market development.

One often hears retail investors complain that they struggle to get into the green-bond market because it is an institutional-investor space. But demand from retail investors is growing. Asset managers have increasingly created green-bond funds that allow these investors access and this will continue.

The number of investors taking ESG considerations into their overall investment processes is expanding and will continue to do so. However, ESG integration is much broader than green bonds. It is important not to be overly simplistic as we think about this because there are many different facets. Just because you integrate ESG factors into your investment process does not mean you have a green-bond fund or a separate mandate to buy green bonds.

Do you see any risk around green assets being ringfenced for green bonds, leaving vanilla bond investors with the secondary assets?

If you look at the evolution of frameworks over the years, you will see that a significant commitment to sustainability over the long term has developed, specifically from the perspective of exactly what issuers are going to include as eligible categories into their overall narratives.

If you are talking about a carbon-intensive issuer, it is true that it could engage in renewable projects but lack an overall sustainability narrative. Likewise, if an issuer has one or two solar projects and issues a green bond but provides no background on its overall commitment or sustainability plan, of course this will be a challenge for the market.

It is clear that some green bonds are structured better than others. However, for issuers that follow the GBPs carefully, and in particular principle two – which covers how a green-bond issuer should "clearly communicate" its "process for project evaluation and selection"– there are guidelines on how to avoid badly structured bonds.

Should more jurisdictions make nonfinancial disclosures or impact reporting compulsory?

The Task Force on Climate-related Financial Disclosures was a great step forward for disclosure and this push is continuing. I welcome and encourage continued improvements in nonfinancial disclosures.

Europe has led in this area. If we look at free markets, we know how much investors value these climate disclosures. Stakeholders will communicate their needs to issuers, and issuers should follow the needs of their investors.

The GBP are voluntary and have progressed quite a way without regulatory engagement. We have a long way to go and many hands will be needed to transition to a low-carbon economy – so we welcome mechanisms to achieve this.

> "The transition to a low-carbon economy requires a multifaceted approach. If we just issue green bonds for wind farms, we are not taking into account the overall transition the economy needs to keep global warming to 1.5 degrees by 2030 based off pre-industrial levels."

What do you see as the big themes for the sustainable-bond market in 2020?

The sustainability-bond label will continue to see strong growth and we will likely see more interest from capex-light issuers. This will include, among use-of-proceeds deals, sustainable procurement as the supply chain is relevant and an important element of corporate sustainability strategy.

The sustainability-linked bond product will also continue to grow in popularity. But sustainability-linked instruments are complementary to green bonds and hence don't really find their way into green-bond funds. This is a crucial point: we do not have to make a choice between one and the other. A variety of instruments are available now and this will continue to grow.

I'd like to see continued uptake of GSS instruments by investors in this region of the world, and by this I mean Asia as well as Australia. I think this is vital. Propelling this forward will be the asset owners demanding change. •

Driving sustainability into financial markets in Australia

Jacki Johnson, adviser to IAG on climate change and sustainability and **Simon O'Connor**, chief executive at Responsible Investment Association of Australasia – co-chairs of the **Australian Sustainable Finance Initiative** (ASFI) – provide an update on the programme's first progress report, released in November 2019.

In 2019, we saw two seemingly innocuous fixed-income transactions in the Australian market. Woolworths raised A$400 million (US$273 million) from 90 institutional investors in April, in what was the first green bond issued by a supermarket operator in Australia. In May, Sydney Airport issued Australia's first syndicated loan linked to sustainability performance, raising A$1.4 billion.

In 10 years' time, we may come to see these transactions as the vanguard of what became a wave of new sustainable-focused debt issuance. The Australian fixed-income market in 2030 is likely to look a lot different from what we see today. We expect that, in 2030, individual green bonds and sustainability-linked bond transactions will have become mainstream – barely raising a ripple in a market where they have become business-as-usual.

How we move from an individual transaction focus to a systemic market change is the focus of ASFI, an initiative led by volunteers that has been established to set out a roadmap for realigning the finance sector to support greater social, environmental and economic outcomes for the country.

Formally established in March 2019, ASFI now has more than 130 individuals representing more than 80 separate organisations working collaboratively to deliver a sustainable finance roadmap for Australia in 2020. In May 2020, ASFI will produce its interim report with a final report to be delivered mid-year.

Led by a steering committee that includes senior executives from the four major banks, superannuation funds, community-owned banks, insurers and civil society, ASFI has established four technical working groups. These are:

- Mobilising capital to deliver on our sustainability challenges and opportunities.
- Creating a more sustainable, resilient

PROGRESS REPORT *CHALLENGES*

These challenges need to be addressed so the sector can properly value risk and make better-informed decisions.

1. Leadership, culture and institutional structures

Financial-services sector leadership is key to ensuring there is appropriate valuing of, and accountability for, sustainability performance and the broader impact of the activities of the financial-services sector across Australian society, the environment and the economy.

2. Community and consumer interests and expectations

All Australians engage with – or are influenced by – the financial-services sector, whether through banking, insurance or investment. However, their level of understanding of the sector and involvement with it varies widely. The sheer reach of the financial-services sector requires a proactive approach to ensuring products and services serve Australians well and adequately meet their needs, interests and expectations.

3. Frameworks, tools and standards

Challenges in decision-making and valuation are closely linked to the frameworks, tools and standards used across the financial-services sector. As the sector grapples with change, new sets of frameworks, tools and standards are required to inform investment, lending and insurance decisions. To ensure long-term financial stability and that social needs are met, it is essential that we align tools, frameworks and standards to manage all risks and embrace opportunities.

4. Decision-making and valuation

The financial-services sector relies heavily on valuation of risk to underpin the investment, lending and insurance decisions being made on a daily basis. Yet limitations with existing valuation tools, mainstream practices and a lack of quality data on environmental and social risks challenge the sector's ability to respond to the new sets of risks and opportunities.

5. Unlocking sustainable finance and allocating capital where it is needed

The financial-services sector plays a key role in supporting a strong and resilient economy and in generating long-term prosperity for Australians through the allocation of capital. There is an urgent need to shift new and existing capital into investments that create and better support sustainable and equitable outcomes for Australian people, our economy, the environment, and investment and trade in the region.

6. Policy, regulation and supervision

There is an important role for policy settings and regulatory guidance and supervision to reinforce factors for sustainable finance. This will assist in setting clear direction for the financial-services sector.

and stable finance system by embedding sustainability into systems, markets, products and services to better account for risk and impact.
- Making better-informed financial decisions by enhancing disclosures and transparency.
- Meeting community and consumer expectations, and putting people at the centre of finance's purpose.

There is also a coordinating working group set up to deliver practical recommendations on overarching and cross-cutting issues not captured in the technical working groups – including short-termism, valuation, taxation, accounting standards and education.

ASFI's progress

In November 2019, ASFI delivered its first publication – a progress report identifying six critical challenges Australia's financial services sector must address (see box on facing page).

The work ASFI is doing is not occurring in a vacuum. Countries around the world have undertaken similar exercises. The reason for this is that nations, including Australia, have signed up to three international agreements: the UN Sustainable Development Goals, the Paris Agreement and the Sendai Framework for Disaster Risk Reduction. All explicitly mention the importance of the finance sector. This focus on finance in international agreements reflects its central role in a nation's economy to meet the scale of the challenges it faces.

For Australia's finance sector, it not only makes sense to align with our society and economy. Because finance is increasingly global, it also makes sense to align with what others are already doing.

Response of fixed-income markets

We are seeing that sustainable finance markets in Australia are experiencing rapid growth and are continuing to adapt and evolve. As of 2018, assets managed in accordance with responsible-investment principles represented 44 per cent or A$980 billion of Australia's A$2.24 trillion in professionally managed assets. This has grown from A$178 billion invested in responsible funds at the end of 2013 which, at the time, represented just 17 per cent of the total assets under management.

Sustainability bond markets – which include green, social and sustainability bonds – are an area where we are seeing change.

JACKI JOHNSON

SIMON O'CONNOR

Cumulative green-bond issuance from Australian entities reached A$15.6 billion as of the first half of calendar 2019. This ranks Australia 10th in the global country rankings. It was third in Asia for 2018 green bond issuance.

Issuers include financial institutions, nonfinancial corporates and state governments, with the latter issuing sustainability bonds to finance projects aimed at delivering environmental and social benefits including transport, renewable-energy, water and low-carbon-building projects.

We are also seeing the evolution of social bonds. The states of Victoria, New South Wales, Queensland and South Australia have issued social impact bonds (SIBs) or conducted SIB pilot programmes aimed at improving particular social outcomes.

There is significant focus on developing SIB markets. In particular, the Australian government has established a Social Impact Investing Taskforce with a view to developing a strategy for the Commonwealth in the social-impact-investing market. One aim of the taskforce is identifying how social-impact investing can provide "additional solutions to address entrenched disadvantage, achieve measurable impact and facilitate private-capital investment".

Implications for investors

One of the core questions ASFI is considering is how to accelerate the rate of development of Australia's sustainable-finance markets.

While there is evidence of market development, is it at a scale that will be required to support Australia to meet the future needs of all Australians and deliver on its international commitments? What practical interventions can be made that can support market development?

There is an opportunity to use the ASFI process to identify and address some of the challenges fixed-income investors face when looking for Australian investment opportunities. Unlike the US, we do not have a deep municipal bond market. Corporate bond issuance is thin compared with the size of the pool of superannuation capital.

Are there also gaps that could be filled through new and innovative investment models? We know, for instance, that social enterprises and community clubs are often unable to finance their needs. Can we learn from the development of securitised debt markets for housing to find new ways to aggregate small-scale projects into investment-scale opportunities?

We recognise that Australia's financial-services sector has traditionally played an important role providing financial services and investment into the region, in particular the Pacific. Challenges remain in allocating capital to economic activity such as infrastructure. Is there an opportunity to explore fixed-income structures and partnerships that can scale and deploy finance in the region?

If we are able to answer questions like these, there is a commercial opportunity for Australia to develop a sustainable-finance market that attracts capital and issuance from around the region.

ASFI is seeking submissions from across the finance sector. If you have an idea about how to support the development of Australia's sustainable-finance markets, we want to hear it. •

Lead from the front

The private sector is the engine of economic activity in Australia and the frontline for lowering emissions. Participants at the UN Environment Programme Finance Initiative (UNEP FI) and UN Principles for Responsible Investment (PRI) conference in Melbourne on 11 December 2019 urged corporates to act on meeting environmental and social challenges – for their businesses and for the planet.

BY MATT ZAUNMAYR

In a June 2019 report from Sustainable Development Solutions Network, Australia ranks 38 out of 162 countries in progress towards the UN Sustainable Development Goals (SDGs).

Australia is among the worst-performing countries in the Organisation for Economic Co-operation and Development (OECD) in this regard, ranking just one position ahead of China and one behind Moldova. Australia performs particularly poorly with regard to SDG 12, for responsible consumption and production, and SDG 13, for climate action.

It is easy to blame federal-government policy malaise for this. And the lack of a policy response certainly has not helped. However, it is becoming broadly accepted that environmental, social and governance (ESG) risk is credit risk and any failure of companies to address such threats their businesses face from a changing climate or increased scrutiny on supply chains is becoming impossible to ignore.

There is now increased understanding that the potential consequences for a business that does not address ESG-related risks may be severe. These include stranded assets, loss in market share, expensive funding and reputational damage.

One challenge Australia faces in addressing ESG-related risk is the concentration of high-carbon industries. Two recent statistics show the obstacles and opportunities confronting companies regarding adaptation to climate change.

The Reserve Bank of Australia's December 2019 *Composition of the Australian Economy* report states that the mining, manufacturing and construction sectors account for 10, eight and six per cent of output, respectively. Meanwhile, the Department of Environment and Energy's *Quarterly Update of Australia's National Greenhouse Gas Inventory: June 2019* shows electricity accounting for 33.8 per cent of total emissions for the year to June 2019, while stationary energy – ie, excluding electricity – and transport each have an 18.9 per cent share, fugitive emissions has a 10.6 per cent share and industrial processes and product have a 6.5 per cent share.

Even so, meeting ESG targets does not have to mean sacrificing financial returns, particularly in the long term. There should be some advantage in being an early adopter of new technologies and practices. If companies do not adapt, they risk being usurped for market share by new players that have emerged to deal with a low-emission operating environment.

URGENT ACTION

On 11 December 2019, a conference hosted by National Australia Bank (NAB) highlighted the necessity of urgent action from corporate Australia in addressing environmental risks. The UNEP FI and PRI organised the event.

PRI chief executive, Fiona Reynolds, set the tone with her opening remarks: "Any company director who is not alarmed by the impact of climate change on people and the economy is out of touch and stakeholders should make this clear. It is our job as investors to deliver returns, but the world our beneficiaries retire into is equally important."

Australian inaction on climate change is not going unnoticed, Reynolds explained, adding that the country is coming up in investor conversations as a sovereign risk. "Australia is the fifth-largest market for the PRI globally, but we have seen little progress on meeting targets such as those in the SDGs or the Paris Agreement," she said.

"Any company director who is not alarmed by the impact of climate change on people and the economy is out of touch and stakeholders should make this clear. It is our job as investors to deliver returns, but the world our beneficiaries retire into is equally important."

FIONA REYNOLDS UN PRINCIPLES FOR RESPONSIBLE INVESTMENT

Only a few companies are getting the point regarding sustainability. Most green, social and sustainable (GSS) bond issuance in Australia has come from semi-governments, global supranational, sovereign and agency issuers, and financial institutions. True corporates have done little.

The proportion of total Australian-market corporate issuance to come in GSS-bond format rose substantially in 2019 (see chart). However, this was primarily on the back of a Kangaroo deal from NextEra Energy and Woolworths' domestic debut, each of which increased total corporate GSS volume by a third.

For the country to make progress in meeting global goals and transition to a low-carbon economy, the emissions-intensive industries that make up the bulk of the Australian economy need to get on the sustainability path.

There have been some advances. The Australian fixed-income market has made strides in product development for ESG funds. Green bonds were first issued in Australia in 2014 and by the end of 2019 just shy of A$21 billion (US$14.2 billion) had been issued in GSS format. Nearly half this total came to market in 2019.

Sustainability-linked loans (SLLs) also grew in prominence for the Australian market in 2019 (see p13).

RISK INFLECTION POINT

The debate around how to transition to a low-carbon economy in Australia has been seen largely through the prism of what would be lost. For example, a common government refrain is that the emissions from coal Australia exports are not Australia's responsibility.

The market community, however, increasingly views ESG as a financial risk. If the world keeps burning coal at its current rate, it will massively overshoot the Paris Agreement goal of limiting global warming to well below 2 degrees celsius over pre-industrial levels. Anyone near the bushfires in New South Wales late last year and into 2020 has a tangible feel for the physical risks of climate change.

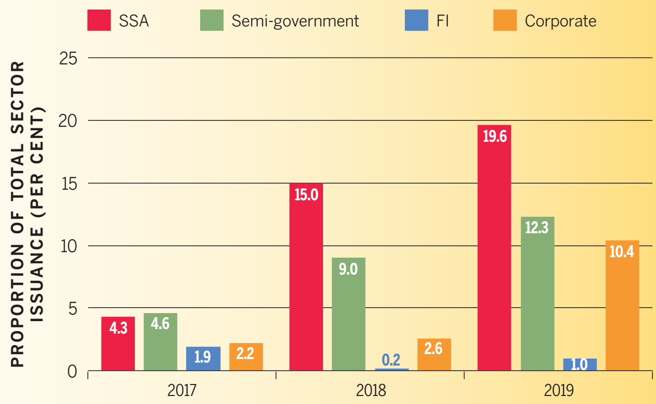
Australian corporates cannot let the government's lethargy influence their decision-making. As Emma Herd, Investor Group on Climate Change chief executive, said at the UNEP FI-PRI conference: "Climate change is an unavoidable financial risk."

The inflection point at which the physical risks of climate change turn into material financial risks might not come until policy action becomes unavoidable for the government. But waiting for this delayed reaction before addressing the risk would not produce an ideal outcome, either.

The inflection point will inevitably be reached, Mark Fulton, founding partner at Energy Transition Partners (ETP), said at the conference. It is merely a matter of when policy action will come and how drastic it will need to be at the point when it does.

Fulton pointed to a survey ETP conducted which found most investors acknowledged there would be a delayed, disruptive policy response to climate change but had not priced it into current risk assessments. When the government does finally take meaningful action, companies that are not acting now to insulate themselves from ESG risk could face stranded assets.

PROPORTION OF AUSTRALIAN BOND MARKET IN GSS FORMAT



SOURCE: KANGANEWS 31 DECEMBER 2019

Those that completely ignore transition requirements may find themselves without customers or cost-effective funding once government, investor and consumer expectations have turned.

Corporates may not be taking this threat seriously. For example, John Thwaites, chairman of Monash Sustainable Development Institute and ClimateWorks Australia, told delegates Australian companies' spending on research and development to assist growth when carbon-intensive activities are no longer viable is already inadequate and going backwards.

It is not just climate-related action that is necessary. The Sustainable Development Solutions Network states that Australia still faces "major" or "significant" challenges in meeting goals on hunger, gender equality, life below land and life on land.

Martin Skancke, board chair for the PRI, told conference delegates that companies have the choice either to take opportunities to transform their existing businesses or not, and their decisions might dictate whether the eventual transition is orderly or abrupt. The latter would be very bad for investors, Skancke said.

HOLDING THE KEYS

If government refuses to incentivise an orderly and timely transition and companies are slow to act, investors and banks can drive change. Just as those that fund Australia's corporate entities have the power to support the growth of companies that are doing the right thing, they can also hold laggards to account.

The debt market is not the only area corporates can access for capital but it is the biggest and the one with the long-term horizons necessary to counter the short-termism that often exists in boardrooms.

Xander den Uyl, PRI board member and trustee at Dutch pension fund APB, told delegates in Melbourne that, using the SDGs as a framework, APB has created a taxonomy under which it aims to invest €58 billion (US$64.7 billion) by the end of 2020. Such frameworks are not only important for encouraging investment, they are also crucial for ensuring the necessary standards of disclosure and transparency (see box on p38).

Reporting: towards a common framework

Disclosure and transparency are fundamental pillars of a legitimate and measurable market for environmental, social and governance (ESG)-related financing. As more Australian companies commit to transition pathways, the challenge will be in measuring sustainability performance and implementing reporting that meets investor requirements.

Speakers at the UN Environment Programme Finance Initiative and Principles for Responsible Investment conference in Melbourne, in December 2019, discussed ways to measure sustainability performance and undertake disclosure reporting. These include applying the UN Sustainable Development Goals (SDGs) to measure performance and the use of Task Force for Climate-related Financial Disclosures (TCFD) reporting.

There has been some progress in Australia. For example, John Thwaites, chairman of Monash Sustainable Development Institute and ClimateWorks Australia, told delegates the proportion of top-50 ASX companies reporting on their progress toward the SDGs is increasing.

The SDGs provide a common framework to measure progress on sustainability and other ESG targets.

Taxonomies and frameworks for sustainable finance are springing up in jurisdictions and from individual investment firms across the world. Market participants often say these are important to ensure targets are locally applicable. However, having these linked to the SDGs or Paris Agreement is also important, to ensure local targets meet global standards.

The EU's *Taxonomy Technical Report*, released in June 2019, states that investors may allocate capital or influence company activities to make a meaningful contribution to climate goals and to the SDGs.

Meanwhile, the heads of sustainability at Australia's major banks have said although TCFD reporting in Australia is still voluntary, it is becoming mandatory for evaluating corporate exposure to risk in the eyes of many domestic investors.

This is at least a good first step. Martin Skancke, board chair of the PRI, told delegates in Melbourne: "The TCFD ensures questions on resilience and governance within companies are being addressed. This is essential in making capital markets work more efficiently to allocate capital to better outcomes."

"The TCFD ensures questions on resilience and governance within companies are being addressed. This is essential in making capital markets work more efficiently to allocate capital to better outcomes."

MARTIN SKANCKE UN PRINCIPLES FOR RESPONSIBLE INVESTMENT

"This taxonomy turns the goals into investment possibilities," den Uyl explained. "It is difficult to quantify how much of the investment would have been made without the taxonomy, but it has made possible the setting of a target for investment and this inevitably channels more funds toward eligible projects."

The pot of money in so-called 'dark-green' funds in Australia is small relative to Europe, so there is probably less incentive for corporate borrowers to target it. This, in part, could explain the corporate sector's lacklustre take-up of GSS bonds. But it is also true that the local corporate bond market is simply not used by a wide swathe of corporate Australia. Plenty of the biggest companies rely on bank loans and global markets. Banks, therefore, have the potential to step in and drive change.

BANKS SIGN UP

A clear sign that some of Australia's banks are ready to encourage the reallocation of capital to achieve sustainable outcomes is their support for the Principles of Responsible Banking (PRB), launched in New York on 23 September 2019 (see p54). The principles require banks to align strategies with the SDGs, the Paris Agreement and relevant national frameworks.

National Australia Bank (NAB) and Westpac Banking Corporation were among 30 global financial institutions that led the development of the PRB. Principle 2 requires banks to set targets to increase positive impact and decrease negative impact. Rosemary Bissett, head of sustainability governance and risk at NAB, told delegates in Melbourne this is where the rubber hits the road in setting targets for lending to companies and projects making a positive contribution.

In the same panel session, Paul Orton, global head of project and export finance at ANZ, said the PRB help determine the companies which ANZ should bank. "We have had conversations with the top-100 carbon-emitting companies we lend to about plans for transitioning to a lower-carbon future. Our customers want us to lead conversations on the SDGs so we can facilitate lending to these activities," Orton said.

Global initiatives such as the PRB and local ones from the likes of the Australian Sustainable Finance Initiative (ASFI) (see p34) could be crucial in mobilising capital for better outcomes. Jacki Johnson, group executive of people, performance and reputation at IAG and co-chair of ASFI, told delegates the Australian economy faces two scenarios going forward. It can either maintain the status quo, leading to a slow decline, or embrace a prosperous future through changed behaviour.

Johnson summed this up for delegates: "The financial system is there to serve society. We need to take action as leaders and not just talk." •

Against a rising tide

The scale of Australia's infrastructure task means investors in the sector are instrumental in driving climate change outcomes. They also recognise that climate-risk assessment is a financial consideration and, therefore, they have a fiduciary obligation in the environmental, social and governance (ESG) arena. If they ignore this, they risk failing to deliver long-term, sustainable returns.

BY CHRIS RICH

Australia's infrastructure sector accounts for almost half the nation's greenhouse-gas emissions, states the Clean Energy Finance Corporation's *Investing in Australia's Infrastructure Sector* report published in May 2018.

Infrastructure fund managers can play a key role in driving change, particularly on climate risk, because they are dealing with long-life assets. As Nicole Bradford, portfolio head, responsible investment at Cbus Super (Cbus) in Sydney, says: "We believe the built environment – including infrastructure – is an enabler of the transition to a lower-carbon world."

Those at the forefront of ESG recognise that focusing on climate risk and other environmental and social issues is not only a fiduciary duty but also the only way to ensure long-term, sustainable returns – particularly given the lasting nature of assets in which they invest.

Bradford says Cbus has an overarching expectation that all managers consider climate-change risk as part of their investment processes. This is particularly important given the youth of Cbus members. "The average age of a Cbus member is currently 39. This means many of our members will be looking to draw an income from their retirement savings after 2050 – when based on current projections the physical risks of climate change will have intensified."

Leisel Moorhead, Brisbane-based partner and ESG champion at QIC Global Infrastructure (QIC GI), adds that managing ESG risk goes hand-in-hand with delivering financial outcomes for clients. "We think infrastructure asset owners have a role to play in delivering a sustainable economy because it is a necessary part of how we deliver long-term, sustainable returns."

Chris Newton, Melbourne-based executive director, responsible investment, at IFM Investors (IFM), agrees. "If we don't manage ESG issues, and climate-related risk specifically, we will not generate long-term returns for our investors. It is opportunity-seeking but ultimately, if we don't do it, our assets will be at risk from a systemic perspective, especially when it comes to climate change."

ESG OVERLAY ON PORTFOLIOS

In response to the challenge of addressing climate-change risks, some large infrastructure investors are implementing portfolio-wide approaches to manage their exposure to threatened assets better.

IFM launched the Australian Infrastructure Carbon Reduction Initiative in August 2019, which aims to reduce its emissions by more than 200,000 tonnes of CO_2 equivalent annually by 2030 across its Australian infrastructure portfolio. The assets in the initiative account for about 90 per cent of the value of the fund's Australian assets. In 2020, IFM will also start work on emissions-reduction targets in its global infrastructure portfolio.

Newton says a guiding principle for setting this target is IFM's responsibility to minimise its own impact on the environment and climate change. "The overlay was doing our bit to meet the Paris Agreement," he explains. "But we then considered what is possible at an asset level that still makes a return – we weren't going to push an option that would be detrimental to our investors."

Cbus released a climate-change position statement in August 2016, followed by the development of a climate-change roadmap

"If we don't manage ESG issues, and climate-related risk specifically, we will not generate long-term returns for our investors. If we don't do it, our assets will be at risk from a systemic perspective, especially when it comes to climate change."

CHRIS NEWTON IFM INVESTORS

to 2020. This identifies the key actions and targets Cbus will implement to move its portfolio in line with the Paris Agreement.

In September 2018, the super fund announced a commitment to net-zero carbon emissions in its property portfolio by 2030. It followed three months later with an announcement that it will be working with its infrastructure managers on their commitments to net-zero targets. During 2019, Cbus worked on assessing climate data for its global quantitative equity portfolio. As a result of these actions, Bradford says, about 25 per cent of the Cbus portfolio is headed toward alignment with the Paris Agreement.

In addition to these commitments, Cbus's investment committee has approved an allocation equivalent to 1 per cent of its default option's funds under management to invest in climate-related opportunities.

The QIC GI fund does not have a target for overall emissions reduction, but this is something the firm is working toward. "We are at the beginning of this journey for our fund as a whole," Moorhead tells *KangaNews*. "We have carbon-footprinted the entire portfolio for the second year in a row. We haven't yet established or calibrated a specific target. But, by doing this work, we are identifying what we may be able to achieve."

Meanwhile, over the last five years QIC GI has been developing and implementing a process to understand and respond to the impact of climate change on its assets. Moorhead says because infrastructure has a particular exposure to the physical risks of climate change, the fund manager started by developing a framework at portfolio level to assess which of these assets are exposed and why.

As Moorhead explains: "There is no one-size-fits-all to climate risk. You have to understand the nature and particular vulnerability of an asset given its location, age and other factors. We did this on a matrix that looked at criticality and vulnerability so we could assess how each of the assets within the portfolio sits on the matrix to help us identify and understand the nature of risks across the portfolio."

Unfortunately, the lack of policy from the federal government around carbon emissions and the environment more generally makes it more difficult for infrastructure investors to make these assessments of environmental risk.

But given the long-term nature of their assets, infrastructure investors are not waiting for government direction. As Bradford says: "We are operating in an environment where ESG isn't radical anymore – it's mainstream and a lot is being done by industry groups and companies independent of legislation. Australian financial regulators continue to speak to the importance of responsible investment being a fiduciary responsibility. We see a future with increasing regulatory scrutiny of how we incorporate risks and opportunities when setting investment strategy as responsible investors, especially around climate change."

One of the tools that helps investors measure climate risk is disclosure. Bradford adds: "We're seeing more companies heading down the road of comprehensive disclosure. The ASX [Australian Securities Exchange] requires continuous disclosure and is encouraging companies with material climate-risk exposure to report against TCFD [Task Force on Climate-related Financial Disclosures] guidelines. This helps investors such as Cbus assess risk, including understanding how companies are managing the transition to net-zero carbon."

ASSET ENGAGEMENT

For infrastructure investors to gauge the risks they face from climate change, and work to make a difference, they need to fully understand both the physical (see box on p42) and financial risks of each individual asset.

One challenge here is the lack of homogeneity in the infrastructure sector. As Moorhead says: "Every asset is at a different level of maturity and faces a different issue. You have to identify what the issues are and prioritise accordingly."

Newton agrees."Once we set the overall objective for the Australian Infrastructure Carbon Reduction Initiative, so we had baselines of emissions profiles, we then started to look at how to reduce our emissions on an asset-by-asset level," he says. "Each of the assets in the portfolio has a sector-specific or asset-specific target."

As a result, IFM has worked with many of its Australian critical infrastructure assets to address emissions intensity. Companies such as Ausgrid, Southern Cross Station, Port of Brisbane and NSW Ports now have emission-reduction targets through to 2030 and beyond. Ausgrid, the largest emitter among the initiative's assets – more than 10 times the second-biggest – has a target of 17 per cent reduction by financial year 2030 based on its baseline year of 2017.

For QIC GI, working out how to mitigate climate risk at the asset level means a focus on resilience. Moorhead says: "It is about ensuring that the assets can get back up and running as soon as possible. After all, infrastructure assets are all about delivering essential services for the community."

> "We are engaging with all our assets to work toward a net-zero carbon target. Once this is in place, you can then calibrate the relevant milestones and understand how best to drive change in the business."
>
> **LEISEL MOORHEAD** QIC GLOBAL INFRASTRUCTURE

STRESS TESTING

Climate change presents a physical, as well as a financial risk to many pieces of critical infrastructure. Investors need to be able to measure these risks to make capital-allocation decisions. This can be difficult, considering the sometimes-distant horizon of climate predictions.

One example of the extended time frames that investors need to take into account for climate impact is the projections on rising sea levels.

The *Special Report on the Ocean and Cryosphere in a Changing Climate*, released in September 2019 by the Intergovernmental Panel on Climate Change, states that even with immediate cuts to carbon emissions, extreme sea-level events that are historically rare – once a century – are projected to occur frequently, and once a year at many locations around the globe, by 2050.

This means heatwaves that increase energy demand and threaten the energy network, and severe storms – like the one that led to a stormwater surge and flooding of two of Sydney Airport's three runways for a day in November 2018 – will become regular occurrences.

IFM Investors (IFM) conducts short-to-medium term stress tests for its assets. But there are issues around forecasting for events that are potentially a long time in the future, says Chris Newton, executive director, responsible investment at IFM.

However, climate events are already providing data that can help manage risk for future events. For example, the bushfires that ravaged New South Wales toward the end of 2019 and into 2020 have a material and current impact on Ausgrid's bushfire management plans to protect its poles, wires and substations.

"Bushfires will increase in severity and duration," Newton says. "This affects the business operationally now. The impact of climate change manifests in how many staff Ausgrid will need to employ to do things like clear land and undertake back-burns."

Leisel Moorhead, partner and ESG champion at QIC Global Infrastructure, adds that it is not just the impact on the assets themselves that should to be taken into account. She points out that climate-related events can also affect surrounding, interconnected services that assets may rely on.

"There is no point having the port open if the main connecting road is flooded, or a renewable generator producing electricity if the network or substation is affected by adverse weather conditions," Moorhead says. "It comes back to operational resilience – making sure you are adapting infrastructure to ensure this."

Stress tests for infrastructure can be built into financial considerations, says Nicole Bradford, portfolio head, responsible investment at Cbus Super. "Our infrastructure fund managers have undertaken physical risk assessments to inform how events could have an impact on our assets. This is a consideration in how costs are factored into the ongoing management of the asset."

The baseline, Moorhead says, is to ensure infrastructure assets are starting to measure their carbon emissions. "We are engaging with all our assets to work towards a net-zero carbon target. Once this is in place we can calibrate the relevant milestones and understand how best to drive change in the business."

To do this, QIC GI practises active asset ownership. "Our approach is to identify and understand the material issues for a particular asset. We then work with companies to understand the climate or carbon risk and identify the transition process."

Moorhead cites the example of Port of Brisbane. "We worked with the company to revitalise its sustainability strategy and we pushed it to produce its first sustainability report using the [UN] Principles for Responsible Investment framework."

Cbus's property fund managers must commit to setting science-based targets for net-zero emissions by 2030. "We believe this will raise standards of the built environment," Bradford says. "We see this as an important reputational matter for property and it is also becoming an area of greater focus for infrastructure companies. We are working closely with all our managers to ensure they have targets in place that are realistic and achievable, while still driving change."

Bradford identifies a significant flow-on effect from setting net-zero targets. "It will stimulate the broader climate-related investment market in green bonds, green financing and renewables," she says.

This deepening of the sustainable-finance market brings another benefit. Matthew Zwi, Sydney-based principal at QIC GI, explains: "We have ongoing dialogue with treasurers and CFOs across our portfolio to discuss how we can incorporate sustainable-finance types of products into their capital structures because we think these can add an additional layer of incentive to meet sustainability targets." •

"We are operating in an environment where ESG isn't radical anymore – it's mainstream and a lot is being done by industry groups and companies independent of legislation."

NICOLE BRADFORD CBUS SUPER

ESG steps forward in rating-agency analysis

The evolution of debt investors' incorporation of environmental, social and governance (ESG) factors is making rating agencies more relevant to the sector. In particular, the move towards incorporating ESG into entity-level credit analysis is bringing the sustainable market into the rating agencies' sweet spot. Challenges in determining materiality and timeframes for risk remain.

BY LAURENCE DAVISON

The global green, social and sustainability (GSS) bond market grew to more than US$200 billion of aggregate issuance in calendar 2018 without developing a specialist niche for the main international rating agencies. While the majority of GSS transactions come from rated issuers, only a relatively small proportion have a rating-agency contribution to their GSS aspect.

For instance, *Environmental Finance* data suggest about 11 per cent of GSS deals completed in 2018 had an external review completed by either S&P Global Ratings (S&P) or Moody's Investors Service (Moody's), while Fitch Ratings (Fitch) was not active in this space. For comparison, the market leader in 2018 – Sustainalytics – provided external review on nearly 20 per cent of GSS bonds.

External review is a crowded field and the traditional rating agencies are staking their claim to market share. But it is the emergence of entity-level – rather than transaction-specific – ESG analysis and scoring that allows rating agencies to deploy their expertise in ESG risk analysis as part of their core business offering.

The rating-agency sector is rapidly moving toward ESG being a fully integrated component of credit analysis, and the pace of evolution is quickening as the time horizons for climate risk, in particular, become increasingly relevant to debt investors. All three main rating agencies say investor demand for this evolution has picked up in the last year or two.

Fitch made a notable move in this space in 2019, by incorporating ESG scoring into all its mainstream credit reports. It describes itself as "the only rating agency at the moment that transparently displays the relevance and materiality of ESG issues in all the ratings we release". Moody's and S&P are far from absent from the ESG space, though. Both have updated the contribution ESG factors make to their overall rating process.

The biggest challenges to full incorporation could be the difficulty of assessing materiality over a medium-term timeframe – especially when public policy is volatile or not fully formed – and the availability and consistency of disclosure.

ESG INCLUSION RATIONALE

All three rating agencies say their moves to greater incorporation of ESG into the mainstream rating process are driven primarily by an increasing understanding that these factors can provide material financial risks in a meaningful timeframe.

For instance, while S&P has been thinking about ESG issues in credit analysis for at least the last 8-10 years, its Sydney-based senior director and sector lead for Pacific corporate and infrastructure ratings, Richard Timbs, says the impetus has clearly grown. He tells *KangaNews*: "Over time, as there has been more evidence about climate change and evolution of social and community expectations, the impact of environmental and social factors on credit has become more regular and more pronounced. For instance, climate-change events are happening more frequently and the impact of these events is more severe."

S&P did a study in 2018, covering the period June 2015 to June 2017. This looked at a sample of about 7,500 global

"Rating agencies are not displaying subcategories of risk sufficiently clearly. We quickly reached the conclusion that calls for this data were not a fad, rather the data forms part of asset managers' requirements and will continue to do so."

ANDREW STEEL FITCH RATINGS

> "It is extremely difficult to factor in the vagaries of public policy. It is extraordinarily difficult to build judgements about policy and pricing into the future or estimates of when certain impacts might occur into a credit assessment."
>
> **RICHARD TIMBS** S&P GLOBAL RATINGS

corporate credit ratings and identified occasions when a credit review or report referred to ESG. The study found that about 15 per cent of the sample had some form of ESG factor and in about 3 per cent of cases an ESG issue was an explicit driver of change in a rating or outlook. About 60 per cent of the changes were negative.

Of the 15 per cent, Timbs says slightly more than half were references to the environment. Within the 3 per cent that were explicit rating drivers, again, half were environmental and about a third related to governance.

INVESTOR DEMAND

The materiality of ESG risk is climbing. It is no surprise rating agencies are also experiencing buy-side demand for more, deeper, more quantifiable and better-embedded ESG analysis. Following a trip down under in July 2019, Andrew Steel, global head of sustainable finance at Fitch in London, told *KangaNews* the catalyst for integrating ESG analysis into its rating process came from the UN Principles for Responsible Investment's initiative for ESG in credit risk and ratings.

This aims to enhance the transparent and systematic integration of ESG factors into credit-risk analysis. "The message that emerged loud and clear was that rating agencies were not displaying subcategories of risk sufficiently clearly," Steel said.

Fitch then spent several months in consultation with asset managers globally to try to ascertain whether they would like to have this information on a permanent and ongoing basis. Steel continued: "We quickly reached the conclusion that calls for this data were not a fad, rather the data forms part of asset managers' requirements and will continue to do so."

There is some debate about whether investor demand for rating agencies to present ESG analysis in their mainstream process is as prevalent in Australia as in, for instance, Europe.

Steel told *KangaNews* his impression was that Australia's buy side is more focused on product, including GSS bonds and sustainability-linked loans, whereas investors globally are further progressed with embedding ESG analysis holistically.

On the other hand, Ilya Serov, associate managing director, structured-finance group and chair, Asia-Pacific ESG working group, at Moody's in Sydney, says: "When I got involved in the ESG field three or four years ago, ESG-related questions from investors came up only infrequently and tended to be pretty high-level. We are now at a point where I'd say probably the majority of investor conversations have an ESG component to them and every organisation we deal with is engaged with the topic."

HOW TO DELIVER ESG ANALYSIS

The way rating agencies deliver ESG analysis varies between the providers. But there are common themes. Naturally enough, the focus is always on risk factors and rated entities' planned response to them. The rating agencies have generally elected to view this through both a sector-level and an entity-specific lens.

Fitch, for instance, reports ESG risk on the basis of a 1-5 score that incorporates sectoral and entity factors (see table 1). Of the first 73,000 individual ESG scores Fitch published – on more than 5,300 publicly rated entities – between January and June 2019, 22 per cent of corporate entities had at least one score of four or five. "This confirms that, from a credit perspective, ESG risk factors are important and material to credit ratings," Steel told *KangaNews*.

Moody's works down from its own ESG taxonomy, to sectoral risk analysis – including estimating the timescale on which risk factors will emerge – to issuer-level assessment.

Moody's has also introduced a specific carbon-transition assessment that ranks issuers on a 1-10 scale – with 1 being the best outcome and 10 the worst – where scores increase as individual entities' ability to deal with regulatory and other environmental risks weakens.

TABLE 1. FITCH RATINGS ESG SCORING DEFINITIONS

LOWEST RELEVANCE		NEUTRAL		CREDIT-RELEVANT TO ISSUER
1	2	3	4	5
Irrelevant to the entity rating and to the sector.	Irrelevant to the entity rating but relevant to the sector.	Minimally relevant to rating: either very low impact or actively managed in a way that results in no impact on the entity.	Relevant to rating: not a key rating driver but has an impact on the rating in combination with other factors.	Highly relevant: a key rating driver that has a significant impact on the rating on an individual basis.

SOURCE: FITCH RATINGS 6 AUGUST 2019

"The rule is generally that there is no fixed rule – we will consider anything we think could affect a company's credit position. This also means we have no set time horizon, be it for ESG or any other factor."

ILYA SEROV MOODY'S INVESTORS SERVICE

In November 2019, Moody's published the results of its carbon-transition analysis of the global automobile manufacturing sector. The median score was CT-6 – slightly below expected average – but Serov says the range of outcomes demonstrates the value of this type of analysis.

S&P looks at business risk profile, including industry risk, alongside specific financial risk factors for an issuer. The first part of this is the industry generally. S&P has been through an exercise of assessing and ranking sectors based on their exposure to environmental and social risks. It then tries to make an assessment of an issuer's exposure to environmental or social issues relative to its peer group.

"The other area we assess is the financial risk profile," Timbs explains. "Where we can make a reasonable assessment into the foreseeable future, we are looking for potential cash-flow impact – good or bad – from specific environmental or social reasons. It is a bit harder to make a material judgement on the social side."

In November 2019, S&P acquired the ESG ratings business from RobeccoSAM. This includes the SAM corporate sustainability assessment (CSA) – an annual evaluation of companies' sustainability practices. S&P says the CSA is "recognised as one of the most advanced ESG scoring methodologies, as it draws upon 20 years of experience analysing sustainability's impact on a company's long-term value creation."

TIMING CHALLENGES

The idea of a reasonable assessment into the foreseeable future speaks to the biggest challenge in ESG analysis as part of the rating process: judging the amount of time before a risk factor becomes material. Timing risks is important in any credit analysis, of course, but environmental and social risks are particularly time sensitive.

This also explains why the equity market has been quicker than fixed income to embrace ESG integration. Equity investors have a perpetual exposure and should therefore consider all factors material to future earnings. Debt investors have a fixed horizon for capital return and can, in theory, ignore risks that do not become material during their exposure period.

Timbs says some debt investors have started thinking about ESG risk from a long-term-hold perspective – they look through future refinancing, in other words. Others have a shorter-term focus. They might be thinking no further than whether an issuer will be able to get its next refinancing away and whether ESG considerations could have an impact on its ability to do so.

"We don't have a hard-and-fast time horizon when we are doing a corporate credit rating," Timbs reveals. "Some market users seem to assume it is three years, and this isn't a bad guideline. But it's still not accurate – it could be two years or it could be four or five. It's really about the level of confidence we have about risk and cash flow over the period of time we are analysing."

The position is similar for Moody's. Serov explains: "The rule is generally that there is no fixed rule – we will consider anything we think could affect a company's credit position. This also means we have no set time horizon, be it for ESG or any other factor."

The challenge is that the further out analysis goes the harder it becomes to assess materiality. Serov continues: "We try to incorporate anything where we think there is sufficient visibility and certainty, even if it is a long-term factor. We give most value to factors on a 1- to 5-year horizon but there is some weight given in the Moody's scorecard to 6-15 years and beyond."

Fitch's approach is slightly more proscriptive. Steel told *KangaNews* that the "vast array" of ESG rating products, from more than 220 providers, are based on a range of very different time frames. But he added: "This can be confusing for asset managers as they try to work out the relative importance of different factors. To provide consistency, we decided to match our scores with our rating time frame – typically a 3-5 year forecast period."

Adding to the complexity is the fact that public policy can have a massive impact on the level of risk ESG factors pose to issuers. It is easier to assess an energy company's planning around emissions transition if it operates in a jurisdiction with a coherent energy policy and a well-established carbon-trading scheme, for instance.

"It is extremely difficult to factor in the vagaries of public policy, and in some cases it is not really possible at all," Timbs comments. "Australian energy policy is a good case in point. It has been fluid for many years and still isn't really clear now. It is extraordinarily difficult to build judgements about policy and pricing into the future or estimates of when certain impacts might occur into a credit assessment."

Serov says "by far the biggest challenge" for ESG analysis is the relevance and quality of data and disclosure. "There are big questions about standardisation and consistency of disclosure across asset classes and jurisdictions. We are grappling with this, because of the extent to which we base our views on public data." •

NAB makes hard commitment to ESG strategy

National Australia Bank (NAB) has transformed the way it confronts environmental, social and governance (ESG) issues across the bank. At heart, this is a move beyond the concept of corporate responsibility as the basis of a sustainability strategy. The bank is now taking a more proactive approach, through a focus on social impact that drives assessment of tangible factors and concrete action.

Perhaps the most critical discussion in sustainable finance today is how financial markets can adapt capital flows to support the transition to a truly sustainable global economy. This means changing the way we view traditional financial capital, a concept that has remained static for decades.

The evolution of NAB's strategy is about understanding the materiality of the transition to a sustainable future economy. It is an active recognition of the challenges involved for such an important aspect of the financial system, but also the opportunities this offers a bank through the transition to a shared-value mindset.

At the heart of this strategy lies a collective understanding of the action needed now to promote a vibrant and sustainable economy in the future. It's not a 'nice to have' or a set of vague aspirational statements. NAB is serious about setting real-world goals and targets, and taking action.

ESTABLISHING A VISION

NAB has taken a leadership position to inform its own strategy. A key piece of work within this context is the *Australian National Outlook 2019* (*ANO*), which combines integrated modelling and research from the Commonwealth Scientific and Industrial Research Organisation (CSIRO) with input from *ANO* participants, a group comprising more than 50 leaders across 22 Australian organisations from industry and the not-for-profit and education sectors.

NAB and CSIRO partnered to deliver this project. The goal is to provide a compelling view of Australia's future, based on new scientific data CSIRO provided that models the future of Australia's natural resources and energy, productivity and services, and cities and infrastructure.

The move to initiate such a wide-ranging piece of work was informed in part by the global discussion on redirecting capital. "Our work on the *ANO* to identify the key shifts that

TABLE 1. AUSTRALIAN NATIONAL OUTLOOK 2019 SCENARIO OUTCOMES BY 2060

ECONOMIC FACTOR	"SLOW DECLINE" OUTCOME	"OUTLOOK VISION" OUTCOME
GDP growth	2.1% a year	2.75-2.8% a year
Increase in urban density	Little change	60-88%
Real wages growth	40%	90%
Fall in urban vehicle kms driven per capita	<25%	33-45%
Net emissions	-11%	Net zero by 2050
Growth in total energy use	61%	6-28%
Growth in real returns to landholders	A$18 billion (US$12.4 billion)	A$42-84 billion
Fall in average household spend on electricity	38%	58-64%
Environmental plantings in 2060	Minimal	11-20 mega hectares

SOURCE: COMMONWEALTH SCIENTIFIC AND INDUSTRIAL RESEARCH ORGANISATION, NATIONAL AUSTRALIA BANK APRIL 2019

"We wanted to focus on the issues where we can make a real difference by leveraging our assets and expertise to contribute to a more healthy and prosperous future for Australia in the long term."

SASHA COURVILLE

need to happen in Australia was very much driven by global trends," explains David Jenkins, NAB's Sydney-based head of sustainable finance. "Our strategy is tailored to our core markets but it has not been developed in isolation."

The offshore developments NAB leveraged include the evolution of the sustainable debt-financing market – such as sustainability-linked lending and transition-financing products. Jenkins confirms that Europe is still leading the market development but there is increasing take-up and engagement in Australia.

The *ANO* identifies two scenarios for the Australian economy in 2060 – the horizon date for the report. One is a "slow decline", which largely maps the expected trajectory of the economy without clear leadership. The other is an "outlook vision", under which the country takes decisive action and a long-term view, and thus achieves much more positive outcomes. The factors identified as contrasts between the two scenarios demonstrate the key role finance can and should play in trying to map the national trajectory to the more positive outcome (see table 1).

The *ANO* also identifies five key areas where its authors believe shifts will be necessary to achieve the positive outcome. The areas are industry, urban, energy, land and culture – and they inform NAB's strategy for the short, medium and long term.

The relevance to a major financial institution of the shifts the report identifies is readily apparent. For instance, the change in technology refers to increasing uptake to boost productivity, investment in skills to ensure a globally competitive workforce in a technology-enabled future and the development of export-facing growth industries.

Even the culture-based changes the *ANO* recommends would have a direct impact on the financial-services sector. These shifts include rebuilding trust and respect in political, business and social institutions, encouraging a healthy culture of risk taking, curiosity and acceptance of fear of failure, and recognising and including social and environmental outcomes in decision-making.

TABLE 2. ALIGNMENT OF NAB'S SOCIAL IMPACT STRATEGY WITH UN SUSTAINABLE DEVELOPMENT GOALS

SOCIAL-IMPACT STRATEGY GOAL	DEFINITION	ALIGNED UN SDG(s)
Financial health	Helping people reduce financial stress and feel more in control of their money.	8. Decent work and economic growth.
Stronger communities	Creating more sustainable, accessible and inclusive communities across Australia.	11. Sustainable cities and communities.
Banking on nature	Driving investment in natural assets to improve community wellbeing.	15. Life on land.
Climate action	Working with communities to ensure they are more resilient to climate change and supporting a low-carbon economy.	7. Affordable and clean energy. 13. Climate action.

SOURCE: NATIONAL AUSTRALIA BANK 2 DECEMBER 2019

DEVELOPING A STRATEGY

What the *ANO* provides is something more than a vision but not quite a roadmap. NAB's social impact strategy and other commitments – including tangible, dollar-value financing commitments – attempt to bridge the distance to the target with a concrete plan of action.

NAB refreshed its social impact strategy in September 2019. The new strategy is a product of the work the bank has done to understand, in a material and meaningful sense, the path to a sustainable and vibrant future economy and its own role in ensuring this path is followed.

"We heavily leveraged the work we had recently completed in partnership with CSIRO on the Australian national outlook," confirms Sasha Courville, general manager, social impact at NAB in Melbourne. "CSIRO's modelling, expertise and the science behind it, together with participation from NAB and 20 other organisations involved in the process, underpinned the conversation about our strategy."

The *ANO* is just one example of the way NAB used real-world analysis to maximise the relevance of its social impact strategy. Courville continues: "We took a step back and looked at everything that is going on in a wider context. We leant heavily on our materiality analysis, which is the product of a very comprehensive process over the past year."

NAB's plan is to use all the tools at its disposal to achieve positive results. Courville explains that this means

TIMING THE RUN: WE MUST KNOW HOW FAR, AND HOW QUICKLY, TO MOVE ON CLIMATE

The clear scientific consensus is that time is running out to arrest a global environmental disaster. When it comes to decisions like exiting the coal sector, an institution such as National Australia Bank (NAB) needs to know not only what to do but also how quickly to move.

"Time horizons are an interesting challenge," admits Sasha Courville, NAB's general manager, social impact. "We have to push ourselves to think in the longer term."

The bank also keeps getting new information. This means a sustainability strategy has to be an iterative, reflexive process that enables NAB to start putting numbers out in the knowledge that it will have to review them as further data emerges, insights are made and policy changes. It has to respond at the same speed at which the understanding of key factors evolves.

Courville adds: "The bank's climate-related announcements in September 2019 include our coal transition pathway, which has an effective exit date. This – as well as our broader strategy – has been informed by modelling. But it is also subject to an annual review."

The *Australian National Outlook 2019* report, on which NAB partnered with the Commonwealth Scientific and Industrial Research Organisation, was extremely helpful in developing the bank's strategy on timing, Courville explains, precisely because it took a very long-term view – out to 2060.

The horizon for the NAB social-impact strategy is shorter. It is a 10-year project. This time frame matches the timeline for the UN Sustainable Development Goals, to which the strategy's four targets have been matched.

Courville explains: "Having an explicit, 10-year time horizon for the social impact strategy is critical, because we have to be able to think, plan and execute in the long term – while of course also having shorter-term goals and milestones. These issues cannot be addressed in a one-year cycle."

leveraging strategic giving and corporate responsibility as well as the shared-value lens as a means of meeting societal needs into the future.

What the bank has produced is an enterprise-wide strategy and not just a product of the sustainability or social impact teams. Different teams within NAB will lead parts of the plan, after the board approved the whole in September. Courville says NAB is putting in place mechanisms to track progress and develop governance structures that will help deliver on the strategy across the organisation.

The social impact strategy aligns with the UN Sustainable Development Goals (SDGs), in particular the five goals NAB has identified as its priorities (see table 2). Once again, this alignment is about focusing NAB's resources where they can have the biggest impact by linking the social impact strategy to the bank's broader ambitions and responsibilities.

"We wanted to work out the areas where we can have a transformative impact and make a contribution to significant change," Courville says. "This doesn't mean we aren't making efforts in other areas. But we wanted to focus on the issues where we can make a real difference by leveraging our assets and expertise to contribute to a more healthy and prosperous future for Australia in the long term."

MAKING A MATERIAL DIFFERENCE

The endgame of NAB's approach is delivering measurable outcomes via quantifiable commitments to a raft of sustainability projects in the social and environmental realms. There are multiple examples from the social impact strategy. The goals of "financial health" and "stronger communities" are just two of these.

One of the measurables in the financial-health sphere is NAB's commitment to provide A$130 million (US$89 million) and NZ$60 million (US$39 million) in capital for microfinance loans to people living on low incomes in Australia and New Zealand. The plan is to continue to build on support for people who are excluded from mainstream finance.

Courville says NAB has also established a framework to support customers who are experiencing vulnerability, an area she describes as "absolutely critical for the Australian banking sector at this moment in time".

This is an area where having an approach based on sustainability and social impact that is deeply embedded across the business is vital. Courville explains: "Vulnerability is situational and it's not something you can tag onto a customer. We have set up a dedicated team to support our people and customers, that provides the special attention and care needed to address how people experiencing vulnerability can interact with their banking and finances."

The financial-health goal also incorporates NAB's work to support older customers and their access to financial services. "We know older customers are much more likely to be the victims of scams and frauds. Proactive engagement and training on our side go a long way to providing a better experience for these customers," Courville says.

In the stronger-communities segment, NAB is building on the *ANO* work to make a commitment of A$2 billion – over three years and across balance-sheet lending, “We need to engage with our customers about how they can put in place material, long-term steps to transition. It’s a two-way partnership. It’s not just a matter of offering financing, even with a cheap cost of funds. It’s more holistic and material than this.”

DAVID JENKINS

capital markets and partnerships – to help increase the supply of affordable and specialist housing in Australia. Categories include crisis accommodation, disability housing, community housing, sustainable developments and build-to-rent properties.

“We really need to understand the issue of affordable housing from an ecosystem perspective, to ensure all the different pieces of the spectrum are working well and needs are being met,” Courville comments. “If one isn’t working, the challenges shift into other parts of the spectrum – in particular crisis accommodation. Our plan is about having appropriate housing for people at the right time and, therefore, focusing on creating longer-term, healthy outcomes for people.”

Jenkins explains that because NAB’s Australian focus is on different parts of the affordable-housing spectrum, the work brings together expertise from right across the bank. “This focus is bank-wide, extending across divisions – it’s not just a corporate and institutional focus area,” he says. “We have established an enterprise-wide council to coordinate our efforts and ensure we’re tackling the challenge as effectively as possible.”

While the focus is on NAB’s home markets of Australia and New Zealand, the bank has also established a presence in UK affordable and social housing. It has provided commitments of more than £500 million (US$658 million) to entities including Sovereign Housing, L&Q Housing and A2Dominion Group as well as bringing Places for People to the Australian and US private placement bond markets and being a joint lead manager on Sovereign Housing’s recent sterling bond deal.

NAB’s commitments also extend to the environmental sector. The bank has committed to providing A$70 billion of environmental financing over 10 years to 2025. Since 2015, NAB has cumulatively provided nearly A$34 billion of this commitment. NAB will halve financing to thermal coal mining by 2028 and intends to be effectively at zero by 2035. NAB will cap its exposure to thermal coal mining at curent levels and will not take on new-to-bank termal coal mining customers. With legacy assets, the focus will be on supporting existing customers across the mining and energy sectors to facilitate an orderly transition to a low-carbon economy.

WORKING WITH CUSTOMERS

The subject of the coal exit poses another question to which NAB has paid significant attention. This concerns an appropriate timeline for moves in the environmental sector, considering the narrowing window available for serious action. As with the *ANO* work, NAB will review targets each year against the latest global climate scenarios and relevant technology developments (see box on p48).

The other issue around environmental transition relates once more to the idea of redirecting capital. This is the extent to which NAB can act not only to reimagine its own business and balance sheet but also its role in assisting customers to evolve to more sustainable business models. “Our own carbon transition is important but by far the biggest role we will play is in supporting our customers in their transitions,” Courville says. “There is a lot of opportunity here, because this work cuts across our entire customer base – around the risks involved with climate change and how they can manage them.”

In the debt market, Jenkins says: “Some companies have been on international roadshows and have been caught unawares by the level of focus on ESG. We have been providing a roadmap of how we have integrated ESG into our internal risk frameworks and sustainability strategy.”

This inevitably leads to a conversation about funding opportunities. After starting this process, Jenkins adds, NAB’s role is to keep working closely with its customers. Communication is key, as is the sharing of knowledge. He says: “We might see resources companies or heavy industrial companies that may not typically be issuers of green or sustainability bonds but are looking to move to more sustainable business models.”

There is risk and opportunity for clients just as much as there is for NAB itself. Jenkins points to increasing investor expectation for greater disclosure on the impacts of climate change and the action to address these. Bond issuers must confront the reality of ESG risk. “This is the tip of the iceberg,” Jenkins says. “This type of action will happen at a far quicker rate, so we need to engage with our customers about why it is happening and how they can put in place material, long-term steps to transition. It’s a two-way partnership. It is not just a matter of offering financing, even with a cheap cost of funds. It is more holistic and material than this.” •

ANZ's future lies in the balance sheet

ANZ is connecting the dots between the asset and liability sides of its balance sheet. It has already transitioned its use-of-proceeds bond issuance to UN Sustainable Development Goals (SDG) format. The bank hopes in future to refinance a much larger pool of sustainability-linked loan (SLL) lending by using these loans to back labelled bond issuance.

Some of the most interesting sustainable-finance work being done by banks globally is around developing a deeper understanding of the whole balance sheet. With a total asset book of nearly A$1 trillion (US$683.1 billion), the scale of a task of this nature is enormous for a bank like ANZ.

The journey is still in its early stages, but ANZ has a clear vision about what it wants to achieve. "It's all about using a funding target linked to the SDGs and our corporate sustainability agenda to really get into the details of how our balance sheet is formed," explains Mark Whelan, group executive, institutional at ANZ in Melbourne.

Katharine Tapley, head of sustainable finance at ANZ in Sydney, adds: "We have had the idea of building our understanding of how the balance sheet fits with concepts of sustainability for a few years. But where we want to take it is much clearer now. We now have the tools to assess and measure our balance sheet in this way."

ANZ has high aspirations when it comes to using the available tools to reshape its balance sheet to match its commitment to sustainability and in particular the SDGs. This includes an expectation of a greatly enhanced link between the bank's corporate purpose, its sustainability goals and its funding programme.

At the heart of ANZ's balance-sheet plans is the evolution of sustainable finance towards a greater understanding of institutional strategy and behaviour. Whether or not use-of-proceeds debt-market products are relevant in the longer term, ANZ's goal is to reflect the work it has done on corporate purpose and the way it measures its performance against those goals (see box on p52) through the balance sheet and funding.

INVESTOR DEMAND

For the foreseeable future, ANZ plans to ramp up its use of SDG bonds within a wholesale funding task that is typically around A$20-25 billion annually. In November 2019, the bank issued its second euro-denominated SDG bond – in tier-two format – to add to the domestic green bond it printed in 2015 (see chart). But ANZ's ambitions are for greatly enhanced issuance volume.

"I want SDG bonds to be a core part of our funding programme in future," says Adrian Went, group treasurer at ANZ in Melbourne. "The fact that the second SDG bond we did was in tier-two format is also significant because tier two is an important part of our funding focus going forward."

It is no coincidence that ANZ's first two SDG bond deals are both euro denominated. Went says European investors have made it clear that this is becoming an increasingly important product not just for SDG funds but also because mainstream funds are moving towards evaluating issuers through an environmental, social and governance (ESG) lens. The SDGs are a commonly used tool for doing so.

ANZ attracted €2.7 billion (US$3 billion) of demand for its latest SDG bond, which printed final volume of

"We're really bringing together the whole story of the momentum behind our corporate policies, our purpose and our business strategy, overlaid with the SDGs as a tool for measurement."

MARK WHELAN

> "We have had the idea of building our understanding of how the balance sheet fits with concepts of sustainability for a few years but where we want to take it is much clearer now. We now have the tools to assess and measure our balance sheet in this way."
>
> **KATHARINE TAPLEY**

€1 billion. The scale of demand was also illustrated by the price revision achieved. Having launched with an indicative margin of 160 basis points over mid-swap the deal priced at 140 basis points over mid-swap. It has also performed well in the secondary market. European investors bought most of the deal but 37 per cent was also sold into Asia.

"Investors are increasingly differentiating between issuers that are strong in the ESG space and those that aren't," Went continues. "Issuing in this format is the right thing for the long-term sustainability of our funding programme because it will ultimately provide access to funding pools that others will not have."

Tapley confirms that investor feedback around the most recent SDG transaction spoke to a much greater degree of sophistication and desire to understand issuers' sustainability credentials, commitments and performance at corporate level. Using SDG deals and their like to indicate that a borrower has a vision around sustainable lending makes these issuers a better risk in the longer term and beyond the confines of a specific bond deal.

"This represents a shift in the way investors are thinking," Tapley adds. "When we did the first SDG deal, which was less than two years ago, discussion with investors was very much about the deal and the specific assets. This time it was much more about what ANZ is doing as a business."

Went adds: "Investors are clearly looking for alignment between the bond itself, the bank's purpose and the bank's overall approach. The buy side doesn't want banks to come to market just because they think it is a good idea to issue this product – they want absolute alignment. The way we have approached this gave us a significant amount of credibility with investors."

European asset managers told ANZ that impact reporting is also important in this context, Went adds. He says a number of investors commented favourably on ANZ's disclosure and transparency relative to other issuers, in part due to its detailed impact reporting.

ANZ has yet to test markets outside Europe for SDG bond demand. Went says Asian interest is growing but remains at a relatively early stage. On the other hand, he reveals: "I'd be very surprised if we didn't do something in SDG format in the domestic market in the near term."

Although ANZ has significant ambitions to grow its qualifying asset base, the relatively limited volume available to date made Europe the obvious place to print the first two SDG deals, especially given the additional-capital format of the second. But Whelan says: "Our team talks to Australian investors frequently and we know there is demand. When we do client roadshows the question of when ANZ is going to do a domestic sustainability issuance often arises."

Tapley adds that there has been a marked acceleration in the Australian investor base in the last 18 months. She says Australian ESG practices are already regarded as relatively sophisticated globally on the buy and sell side, thanks to the quality of deals in the local market and the sophistication of thinking among Australian asset owners.

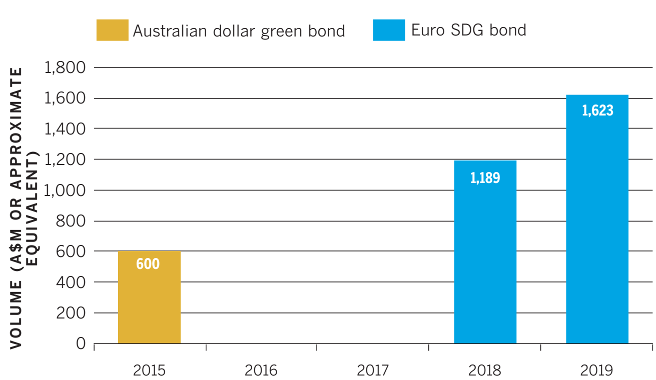
THE FUNDING NEXUS

Plugging in to developments in the global debt market, in and of itself, provides an incentive for ANZ further to overhaul its balance sheet. "The scale of issuance ambitions we have means the institutional team needs to make sure it's writing the assets we need to be able to issue this product," Went comments.

This is about much more than just generating qualifying assets to provide an in-demand product, however. The way ANZ is thinking about ESG across its balance sheet makes the treasury function part of a nexus of factors that have mutual and additive benefits for the overall transition.

SLLs are at the front line of growth. ANZ has huge hopes for SLL growth, having written Australia's first bilateral facility at the end of 2018 and been a sustainability coordinator and

ANZ BANKING GROUP GSS BOND ISSUANCE



SOURCE: KANGANEWS 10 DECEMBER 2019

STARTING POINT: ANZ'S STRATEGY AND PURPOSE

Debt investors globally, and especially in Europe, are increasingly keen to get to grips with borrowers' environmental, social and governance (ESG) credentials on an institutional basis. ANZ believes it has strong foundations to meet buy-side expectations.

This starts with overall corporate strategy, which is "to promote the financial wellbeing" of the bank's customers. Feeding into this is ANZ's purpose, which is "to shape a world where people and communities thrive". One of the ways ANZ is bringing its purpose to life is through action on complex issues that matter to society and are core to the bank's business strategy. ANZ is focusing its efforts on financial wellbeing, environmental sustainability and housing.

ANZ sets public sustainability targets which are approved by the Board Ethics, Environment, Social and Governance Committee. Impact and materiality are critical considerations for investors and other stakeholders, so the bank maps its material issues and sustainability targets to the UN Sustainable Development Goals (SDGs).

Alongside the 17 SDGs are 169 targets aimed at solving the world's most pressing sustainable-development challenges: ending global poverty, protecting the planet and ensuring human rights. Since 2018, ANZ has enhanced the detail of this mapping in its annual ESG supplement.

"We are digging down under the goals to the relevant targets in our reporting," says Anna Stewart, head of corporate sustainability at ANZ in Melbourne. "We do this to give stakeholders greater clarity on which of those targets we seek to have an impact on. We hope this will provide the ability to aggregate up information not only on what ANZ is doing but also the finance sector in general."

Many of the SDGs have some relevance to ANZ and it aligns at least some of its targets with more than half the goals. A number of the SDGs fit especially well with the bank's priority areas. SDG 11, sustainable cities and communities, maps to ANZ's housing targets. Financial wellbeing is another focus for the bank and these targets tend to fall under SDG 1, no poverty. Environmental sustainability targets around renewable energy are also high on ANZ's agenda, matched to SDG 7, affordable and clean energy.

"Another area of focus is gender diversity and equality – SDG 5. We have had gender targets in place for some years now. We also have employment targets for under-represented groups, such as people with disability, refugees and Aboriginal and Torres Strait Islanders," says Stewart.

The goals are broad but by mapping them to specific targets ANZ aims to address materiality. Stewart explains: "We are conscious of 'SDG washing' – it is easy just to align things to the SDGs, put the SDG logo on and be done with it. This is not our intention, which is why our approach is not just about reporting but also the targets we are setting."

ANZ's focus on housing provides an example of the path from aspirational goal to real-world commitment. Stewart explains that housing is a relatively new focus for ANZ in the ESG space and it finalised its first suite of public targets in the sector in 2018. "One of our primary aims is to increase housing supply," she says. "We have a target to develop more affordable, sustainable homes for people. SDG target 11.1 is to ensure access for all to adequate, safe and affordable housing by 2030. There is direct alignment with what we are doing."

To this end, ANZ has arranged three social bonds related to housing, one for National Housing Finance and Investment Corporation in Australia and two deals for Kāinga Ora – Homes and Communities in New Zealand. Stewart says: "These are a real, direct example of how we are aligning our sustainability and strategic business objectives."

"We are conscious of 'SDG washing' – it is easy just to align things to the SDGs, put the SDG logo on and be done with it. This is not our intention, which is why our approach is not just about the reporting we do but also the targets we are setting."

ANNA STEWART

joint bookrunner on the first fully syndicated transaction in May 2019. The two deals were a A$50 million loan to Adelaide Airport and a A$1.4 syndication for Sydney Airport.

The market should expect to see a lot more lending in this format. Tapley believes it will comfortably eclipse use-of-proceeds bond issuance, adding that the scale of demand for SLLs from ANZ's corporate client base is vast.

A bigger SLL book could be a major source of the assets Went wants to fund in the SDG bond space. "One thing I'd like to test with the market is using sustainability bonds to refinance our SLLs," Tapley says. "At the moment we have A$1 billion of our balance sheet in SLLs but that's only going to grow – customer appetite for these types of transactions is uncontrollable. We are very well placed to continue to lend in this format right across our networks in Australia, New Zealand and abroad. It makes perfect sense to use our bond programmes, with some tweaking, to recapitalise this portfolio of loans."

"Investors are clearly looking for alignment between the bond itself, the bank's purpose and the bank's overall approach. They don't want banks to come to market just because they think it's a good idea to issue this product – they want absolute alignment."

ADRIAN WENT

The untested aspect is the linkage of assets that are not explicitly designated for specific projects – a large part of the appeal of SLLs to borrowers is the fact that they can be used for general corporate purposes rather than being tethered to assets – with use-of-proceeds bonds like ANZ's SDG programme.

This question may resolve itself in time, by one of two methods. The first is the possibility that capital markets will transition to assessing issuers' ESG credentials entirely separately from the lens of labelled transactions – in effect making green, social and sustainability bonds redundant. The second could be the continued development of a bond that more closely mirrors the SLL, moving away from pure use of proceeds and towards variable cost of funds based on issuer-level sustainability KPIs.

The SDG programme certainly remains relevant at present, however. Tapley says: "There will still be a place in the medium term for use-of-proceeds transactions. But I can foresee deals emerging quite soon where the sustainability element is linked to the performance of the borrower and not so much to specific underlying assets."

DEEPER IN THE BALANCE SHEET

So far, ANZ's balance-sheet transition is focused on the institutional sector. This is no surprise: institutional clients tend to have sustainability agendas of their own, while institutional assets are easier to analyse and tag for impact and materiality. But ANZ's ambition does not end here.

Perhaps most notably, the bank has a mortgage book of more than A$250 billion and Tapley says there is "a lot of potential for innovation on the mortgage product side" across the market – including, though not limited to, ANZ.

Product development would probably require building codes to be addressed in Australia. But Tapley says really good work is being done by the Green Building Council of Australia, the Property Council of Australia and the Infrastructure Sustainability Council of Australia to develop standards in the residential sector that would help create the framework needed to generate green mortgages and, in turn, structure funding off the back of them.

ANZ already offers a brace of green mortgage products in New Zealand. Healthier Homes has a target to provide NZ$100 million (US$65.6 million) of interest-free loans to mortgage holders for home insulation. The other product offers a rate discount if the borrower builds or renovates to a minimum of six stars under Green Building Council of New Zealand standards.

"Anecdotally, we have been told that ever since ANZ announced this target the Homestar assessors around New Zealand have experienced a marked uptick in enquiries about the rating tool," Tapley reveals.

Elsewhere, ANZ has committed a lot of forward-looking lending to the commercial agriculture sector in Australia and New Zealand. This will be a focus for the bank's A$50 billion sustainable-lending target as well as providing potential assets for SDG bond issuance.

The scale of actual and potential asset growth is dizzying. Even without considering the mortgage book, the bank's A$50 billion target for environmental and social lending by 2025 already marks a major step up. The original target set in 2015 was A$15 billion of lending by 2020 but the bank comfortably surpassed this during 2019, reaching A$19.1 billion by 30 September.

"We expected this would happen so we started conversations in the middle of the year around the next iteration of the target," Whelan says. "We knew we wanted a bigger number and a broader target – it had to cover more than just what the A$15 billion target was covering, which was focused on low carbon and environmental sustainability."

The enhanced lending target covers all three priority areas and also introduces alignment to the SDGs. "We're really bringing together the whole story of the momentum behind our corporate policies, our purpose and our business strategy, overlaid with the SDGs as a tool for measurement," Whelan adds.

Activity in the institutional bank is accelerating even ahead of the expected explosion of transaction flow in the SLL space. Tapley says her business completed eight deals in the financial year ending 30 September 2018, a further 25 in the next 12 months and had already done 12 between 1 October and mid-December 2019.

The strategy goes beyond ANZ's own balance sheet, too. Another area the bank is studying closely is sustainable supply chains. "We want to think about how we can work with corporate or institutional customers with deep supply chains," Whelan explains. "For example, in the construction sector there could be opportunities to create vendor-financing products that incentivise prodution of products like lower-carbon cement and lower-carbon steel." •

Global collaboration critical to banking sector goals

The way Australian companies, especially in the financial sector, are responding to environmental and social risks is becoming more sophisticated and more prominent. **Siobhan Toohill**, group head of sustainability at **Westpac Banking Corporation** (Westpac) in Sydney, says collaboration between industry participants is taking progress to a new level.

The collaborative mindset that is increasingly emerging in the local and global banking community marks a sea change that is unique to the sustainability sector, Toohill says. "There has been a realisation that if we are going to get this right, we have to work collectively to address this substantial problem."

The new mentality, Toohill adds, is that of "a rising tide lifts all boats". Whether it is around climate change in Europe or the response to modern slavery in Australia, a spirit of collaboration is on the rise.

In Australia, for example, the Australian Banking Association now has a sustainability working group which includes the heads of sustainability from the big four as well as regional banks. This group comes together several times a year to discuss key issues affecting the industry such as climate change and Australian banks' work around the Modern Slavery Act. The banks are also looking at how they can collaborate better around ways they can help stakeholders – including customers (see box on p56) – better compare sustainability performance.

"I'm really excited about this openness and willingness of banks to adopt common fundamentals and a common way to engage with regulators around environmental, social and governance (ESG) risks, such as the Task Force on Climate-related Financial Disclosures (TCFD) framework," Toohill continues. "It's powerful that multiple banks have adopted the TCFD – it will really lift the Australian banks to have a more common approach to measurement of climate risk."

ORIGIN OF COLLABORATION

A growing need to measure and disclose the material nature of risk and response has been at the heart of the growth of collaboration in the financial sector. According to Toohill, the role played by the TCFD since its conception in 2015 has had a profound effect across financial markets in this context.

The TCFD laid out an expectation that companies should be reporting on climate risk. This means quantifying and measuring it, setting targets, putting in place relevant governance mechanisms and a general significant increase in focus on the topic.

The TCFD principles initially gained traction in the EU but have now spread globally. In some jurisdictions they are regulated but in others – like Australia – the process remains principles-based. This is not to say TCFD lacks power, though: the mood of 'if not, why not' comes from regulators, the stock exchange and also – perhaps most strongly – from shareholders and other investors.

"We are now seeing the mainstreaming of climate-risk awareness and response happening in lots of different ways," Toohill says. "Within businesses and from investor engagement, the level of maturity in the conversation is increasing as the level of assessment of private risk improves."

The market has not yet reached its final form. Institutions are still working through different models while the capacity to measure and quantify risk varies. But, Toohill says, one of the most interesting things to observe through the process of TCFD adoption has been the discussions that have emerged within the financial sector.

THE ROLE OF THE PRB

Globally, the UN Principles for Responsible Banking (PRB) is a key initiative for collaboration between banks. These principles were established at the start of 2018 with 11 banks from around the world involved – a list that included Westpac. The number of participating institutions had grown to 30 by the end of 2018. By the official launch of the PRB in September 2019 there were 130 participating banks from 49 countries – representing more than US$47 trillion in assets or approximately a third of the global banking system.

The first of the six PRBs (see table) covers alignment of banks' strategic purpose with the Paris Agreement and the UN Sustainable Development Goals (SDGs). Other principles cover impact and target setting, working with clients, customers and other stakeholders to achieve sustainability goals, governance and corporate culture, and transparency and accountability.

Integral to all these principles is the idea of progressing together, as an industry, to achieve specific targets. The PRB and the collaborative environment around them can also support banks at different stages on their journies.

Toohill explains: "There was initially concern, as we were developing the principles, that they would play well for a bank that's quite mature in its sustainability journey but not be so helpful for banks that are just starting out. In designing the principles, we have worked with the expectation that they are about where you are today but also your ambitions for the future. The expectation of the principles is that you are constantly demonstrating improvement and lifting ambition."

The expectation is that banks should constantly be pushing themselves and also – by engagement through initiatives like the UN Environment Programme (UNEP) Climate Initiative and UNEP Finance Initiative (UNEP FI) – that there should be a significant degree of collaboration and learning from each other. "The ability to connect and engage with international banks – to learn from them – has been quite an extraordinary by-product of participating in the PRBs," Toohill confirms.

This outcome was not a central component of the original conception of the PRB. Toohill tells *KangaNews*: "I don't think we realised when drafting the principles that this kind of global collaboration would emerge. But what we have seen is that learning about global best practice is a key means of delivering the goals we have set ourselves. This can be formally, via UNEP FI, but also informally – we pick up the phone to our international counterparts to work together to drive change."

GLOBAL LEADERSHIP

Toohill notes, for example, the positive experience of working with some European banks that have developed a longer-term approach to finance that factors in climate risk. Westpac has had the opportunity to look at the methodologies these banks are using to examine their own portfolios.

Two examples that have been relevant to banks in Australia both relate to European banks working to develop a better understanding of the environmental impact of their balance sheets.

One is ING's 'Terra' approach, which deploys an innovative means of measuring the climate impact of the sectors in the bank's loan book that are responsible for most greenhouse gas emissions: power generation, fossil fuels, automotive, shipping, aviation, steel, cement, residential mortgages and commercial real estate. ING has rolled out Terra on the basis that it wants more entities in the financial sector collaborating and improving data quality to drive greater change.

THE PRINCIPLES FOR RESPONSIBLE BANKING

PRINCIPLE 1 **ALIGNMENT** We will align our business strategy to be consistent with and contribute to individuals' needs and society's goals, as expressed in the UN Sustainable Development Goals, the Paris Climate Agreement and relevant national and regional frameworks.	PRINCIPLE 2 **IMPACT & TARGET SETTING** We will continuously increase our positive impacts while reducing the negative impacts on, and managing risks to, people and environment resulting from our activities, products and services. To this end, we will set and publish targets where we can have the most significant impacts.	PRINCIPLE 3 **CLIENTS & CUSTOMERS** We will work responsibly with our clients and our customers to encourage sustainable practices and enable economic activities that create shared prosperity for current and future generations.
PRINCIPLE 4 **STAKEHOLDERS** We will proactively and responsibly consult, engage and partner with relevant stakeholders to achieve society's goals.	PRINCIPLE 5 **GOVERNANCE & CULTURE** We will implement our commitment to these principles through effective governance and a culture of responsible banking.	PRINCIPLE 6 **TRANSPARENCY & ACCOUNTABILITY** We will periodically review our individual and collective implementation of these principles and be transparent about and accountable for our positive and negative impacts and our contribution to society's goals.

SOURCE: PRINCIPLES FOR RESPONSIBLE BANKING 22 SEPTEMBER 2019

BRINGING CUSTOMERS ALONG *ON THE ESG JOURNEY*

Banks' drive to incorporate environmental, social and governance (ESG) factors in their strategies and day-to-day operations is accompanied by a desire to help their customers' ESG journeys. For the most part, this means facilitating transition rather than outright divestment.

"Our view is that any bank that is quite practised in sustainability has an important role in supporting customers to develop their transition strategies, and to work with customers to use sustainable finance to achieve these outcomes," says Siobhan Toohill, group head of sustainability at Westpac Banking Corporation (Westpac).

This may mean withdrawing support for certain industries or sectors. For example, Westpac cannot see an acceptable transition path for tobacco to achieve a better sustainability outcome so it no longer lends to tobacco companies.

On the other hand, the bank is much more focused on working with companies to incentivise positive transition when it comes to climate change and risk. It has prioritised working with companies that have significant carbon exposure to progress towards a positive transition trajectory.

This is where sustainable finance comes into play in the biggest way – the idea of financing companies, often through Westpac Institutional Bank, to make the investments required to change their positioning around environmental risk.

This could mean lending in sustainability-linked loan (SLL) format, which offers a stick-and-carrot approach to borrowers by incorporating variable pricing in the debt structure based on the company's success or otherwise in achieving sustainability targets.

Another dimension of ESG risk assessment is the wider conversations Westpac is having, and the application of policies and position statements, around climate change, fossil fuels and other aspects of sustainability performance.

Toohill gives the example of lending in the agricultural sector, where Westpac is actively discussing responsible approaches to agriculture and the changes companies in the space are seeking to achieve. "Often driving change is about the conversations you have directly with a customer," Toohill reveals.

"For instance, if it's a customer that operates in a sensitive sector regarding human rights, we will encourage it to put in place an effective policy and some assurance around how it implements that policy. The idea is to create a shift or transition in the organisation to embrace an aspect that will then de-risk the business for them and for us."

In a sustainable-finance world where quantitative targets are becoming increasingly prominent, Toohill agrees that the SLL product is an exciting development.

At the same time, she adds: "While it is vital to talk about the numbers and demonstrate achievements around sustainability targets, the background is how entities manage ESG risk in general terms. I think the correct approach for a bank is to have quantifiable criteria but also to have in place some soft criteria around where it would like to see customers heading."

The other is Natixis's 'green weighting factor'. The bank's representatives visited Australia within weeks of the September 2019 launch of this initiative to spread the word about how Natixis is attempting to monitor and manage the climate impact of its whole balance sheet.

"The work itself is really interesting but what's almost more encouraging is the openness these banks are displaying around sharing their methodologies," Toohill comments. "They have taken the view that leadership is about sharing what they do and supporting more banks to progress."

AUSTRALIA'S CONTRIBUTION

European banks are the acknowledged market leader in environmental transition in particular. But this does not mean the Australian banking sector can only be a follower. The social component of the ESG universe is notably underdeveloped and Toohill believes the opportunity exists for Australia to take global leadership in this area.

To take just one example, the social-bond market is tiny compared with green-bond issuance. *Environmental Finance* data indicate that global green-bond issuance reached around US$170 billion equivalent in 2018, while there was less than US$15 billion equivalent of social-bond volume. Sustainability bonds – which combine environmental and social projects – added US$18 billion equivalent to the total.

One of the biggest reasons for the limited supply of social bonds is the relative complexity of measuring and assessing social outcomes. In the environmental space, it is relatively easy to measure reduced emissions once a baseline standard has been agreed. The same cannot be said for social projects.

Toohill says one of the goals of the Australian Sustainable Finance Initiative (ASFI), which was launched in March 2019 (see p34), is to provide leadership on social impact assessment. Toohill notes that ASFI's co-chair, Jacki Johnson, has said the EU taxonomy is focused on green and climate factors. Australia is somewhat behind the curve in developing a green or climate taxonomy, Toohill acknowledges – but it can make a lead contribution on adding social-impact dimensions to its taxonomy.

"The whole world is still learning how to quantify, measure and set standards around social impact," she says. "It's really significant that Australia is having this conversation and looking to how to build its taxonomy across the SDGs and not just focus on climate."

It is, of course, also critical to have positive impacts to measure. Westpac itself has done a lot of work in the past year in the area of customer vulnerability. The bank has established a customer vulnerability position statement and action plan to set out its approach to providing support to customers experiencing vulnerability. This includes customers who are experiencing domestic violence or elder abuse, or who have fallen victim to scams.

Westpac now has specialist teams across different parts of the organisation to support bankers with complex customer queries. This includes a dedicated Priority Assist line staffed by specialists where customers experiencing vulnerability can access dedicated support and have their issues dealt with appropriately and – just as importantly – promptly.

Toohill explains: "We have uncovered that with vulnerability comes complex claims that can get stuck in the system. We are trying to flip this on its head, to make sure these people are assessed and supported and we can close out their complaints as quickly as we can. To do this we have people who have specialist training to assist people experiencing vulnerability."

Westpac has also introduced a substantive focus on indigenous customers, particularly those in remote areas. Initiatives introduced over the past year include pop-up branches in remote locations."Members of some communities in remote areas rarely make it into a town, they may not have access to cars, they can have problems around identification and verification, and even a mobile phone might be shared by various people," Toohill explains.

"By taking a pop-up branch into remote areas, we are able to offer banking services and also improve people's financial capabilities by having conversations in the moment around banking basics. While this might seem quite a small offering, the impact can be incredibly significant."

Also in the past year, Westpac has set up dedicated customer support teams for indigenous Australians living in remote areas. These customers can now ring a dedicated number and access a specialist team to assist them with their banking needs. The teams are tuned in to the specific types of requirements these customers have, Toohill explains. They will often use a local language and they understand that phones might be shared. The goal is to support these customers in a timely and culturally appropriate way.

"This is one of the things I am most proud of being associated with during 2019. It's the simple things – like helping customers reset pin numbers and checking that customers have the right bank account for their needs – that are having a very profound effect," Toohill comments.

UNIQUE CHALLENGES

The nature of Australian banks' business models also gives them a slightly different perspective from some of the global ESG leaders. "The Australian banks have a particular a focus on social issues, including financial capability," Toohill suggests.

This feeds back into the theme of international collaboration between banks. For example, UK banks also tend to have a focus on customer vulnerability and, according to Toohill, there was significant engagement on the topic between the Australian and UK banks during 2019.

There can be little doubt that the collaborative approach will become even more crucial as the time horizons for a massive increase in action around climate change in particular shrink.

Toohill notes the progress global banks have already made on sustainability product development – including, on Westpac's part, the work the bank did in 2018 on green deposits, which was a world first. In November 2018, Westpac launched a green tailored deposit certified by the Climate Bonds Initiative. It is designed for investors who want investments that genuinely contribute to addressing climate change.

The pace of work on transition is accelerating. Westpac issued its most recent climate-change position statement in 2017 and is due to update this in 2020.

"The more we learn, the more we strengthen our approach," Toohill claims. "As we collaborate more, understand more and undertake more research, the more action we're taking towards the ambitions of the Paris Agreement and the SDGs – not only about managing the risks, but also in new financing opportunities. I am already seeing an acceleration in engagement rippling through the finance sector globally." •

"We are now seeing the mainstreaming of climate-risk awareness and response happening in lots of different ways. Within businesses and from investor engagement, the level of maturity in the conversation is increasing as the level of assessment of private risk improves as well."

SIOBHAN TOOHILL

SUSTAINABLE FINANCE HEADS TO THE MAINSTREAM

Australia has come a long way in the evolution of sustainable finance. Participants at the annual roundtable for the *KangaNews Investing with Impact Yearbook* agree that the conversation is moving towards a holistic assessment of environmental, social and governance (ESG) performance as opposed to a narrow focus on use-of-proceeds products. There is also bigger emphasis on transition in the sustainable-finance sector – a highly salient topic for the Australian economy. This could help further broaden the universe of entities that will work on integrating sustainability into their business practices.

PARTICIPANTS

■ **Michael Chen** Head of Sustainability WESTPAC BANKING CORPORATION ■ **Aziz Dean** Global Head of Debt Products WESTPAC BANKING CORPORATION
■ **David Jenkins** Head of Sustainable Finance NATIONAL AUSTRALIA BANK ■ **Scott Mitchell** Head of Funding NATIONAL AUSTRALIA BANK
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GSS BONDS

Zaunmayr With recent deals, total green, social and sustainability (GSS) bond issuance for 2019 has surpassed A$10 billion (US$6.8 billion). But is take-up as wide as it could be among issuers and investors?

■ **DEAN** We are seeing more and more of our clients – borrowers and investors – showing interest. Even some Asian investors, whether they are banks or funds, are showing interest in sustainable finance.

In the traditional market, we often see companies borrowing from their banks and then doing a bond. What I think we will see develop is issuers doing a sustainability-linked loan (SLL) and then refinancing via a GSS bond. Borrowers can get a bespoke loan that suits their profile and industry, and which they could structure to meet the targets required.

I don't see further market development being about issuers either doing SLLs or GSS bonds. I think it will be both.

■ **CHEN** I like to look at this in terms of segments of issuers, like corporates, semi-governments and banks. The banks were the first movers in Australia and all are actively looking at the market. The only constraint is the availability of assets.

Semi-governments have all talked publicly about the states' major infrastructure task. Some are even bringing this capex forward and are looking to refinance through the GSS bond market, which is pleasing. A lot of the physical and social infrastructure spending by the states, like public transport and eductation, lends itself well to the green and social categories. We should continue to see large-volume deals.

It's a different story for corporates. There is always interest, but whether this translates into deals is a separate matter. Clients are getting closer, though – and there is much interest.

A couple of years ago, the sense was that transaction costs for GSS bonds would be too high and the process too resource intensive. This has changed: now there is a sense that corporates want to be involved and it is a case of looking at how they can.

Cost is no longer the barrier. It is more about internal resources and having sufficient assets for GSS bonds. Also, as we get more sector definitions – beyond renewable energy, buildings and low-carbon transport – there will be more eligible green and social assets. This will open up the market to more potential issuers.

■ **JENKINS** November 2019 was the outlier for issuance. There were 10 transactions for almost A$4 billion, which alone is more than half the total issued in the GSS market in 2018.

Through the early part of 2019, there was possibly some trepidation from new issuers around coming to the GSS market. But there have now been some good examples of new issuers in the market, including international banks like MUFG [Mitsubishi UFJ Financial Group] and OCBC

[Oversea-Chinese Banking Corporation] through its Sydney branch. NextEra Energy has also come to the Australian dollar market in Kangaroo format, as well as National Housing Finance and Investment Corporation (NHFIC) and flexigroup, which brought two green securitisation deals in 2019.

It took a while to establish comfort about the depth of demand in Australia. But the deals done so far have been well supported. It is disappointing that the corporate sector has been slow to issue, but engagement from issuers and investors has increased dramatically – domestically and offshore.

From National Australia Bank (NAB)'s perspective as an issuer of GSS debt, 2018 was a breakout year. We raised more than A$2.5 billion across four green bonds we brought to market in a range of currencies and formats. We then followed up with the uBank retail green term deposit, launched in early 2019.

Swiss Why has corporate issuance lagged?

JENKINS One limiting factor has been resources. The issuers that have come to market have usually been those that are already well down the path of integrating sustainability across their businesses. Issuing a GSS bond aligns with their strategies and makes sense for these issuers.

Corporates that are focused on issuance costs in isolation from their broader sustainability strategies will face challenges. We find that things start happening when treasury teams, C-suite and sustainability teams are integrated and working together.

TAPLEY I agree with Michael Chen that the cost piece is disappearing from the marketplace. We know C-suites have shifted their mindset around climate change and sustainable development. On the other hand, use-of-proceeds borrowing is quite challenging for most corporates because they need to have a substantial asset base. Particular sectors – such as property, low-carbon transport, renewable energy and certain other types of infrastructure – will always lend themselves to use-of-proceeds transactions.

It is morphing, though, more into a greater focus on sustainability. This will propel these markets forward, through the growth of products like SLLs, which we have seen emerge in the Australian market in 2019.

The investor market is becoming more sophisticated. It is no longer just about the transaction and how funds are being used. It is more about what the borrower stands for and how the transaction matches with the company's overall sustainability strategy.

DEAN When it comes to loan product and sustainable finance, we are often asked why there is not a secondary loan market in Australia. The reason is we never really needed one – there has never been a real driver for it.

However, I think sustainable finance could be the trigger for a real secondary loan market in Australia because demand for sustainability-linked loans is not just price-driven. There is a whole different complexion because it is also driven by behaviour and shareholders.

WHITE The level of borrower interest really depends on the sector and the client. But we often have meetings where our sustainable finance team joins the debt-capital-markets team.

In the more liquid part of the market, 2019 has been a very positive year with a lot of issuance from supranational, sovereign and agency (SSA) issuers and semi-government borrowers. As David Jenkins mentions, there has also been

"I think sustainable finance could be the trigger for a real secondary loan market in Australia because demand for sustainability-linked loans is not just price-driven. There is a whole different complexion because it is also driven by behaviour and shareholders."

AZIZ DEAN WESTPAC BANKING CORPORATION

ASSET CONSTRAINTS

Australian banks say the biggest limitation on their ability to issue green, social and sustainability (GSS) bonds is the scale of suitable assets on their balance sheets. In this context, deploying assets in the most productive areas is key.

SWISS How limited are banks by the volume of assets they have to support GSS issuance?

■ **MITCHELL** We have finite capacity. If we could issue A$2 billion (US$1.4 billion) of GSS bonds every year, we would. Bond issuance is a great demonstration of what the bank is doing in the GSS space and also demonstrates our credentials to investors globally. It is becoming an increasingly relevant topic.

Given we have been so active in the space over the last two years it comes down to being able continually to generate the collateral. Our product offering regarding green and social overlays is evolving on the liability side, for example through the uBank green term deposit. We are deploying our collateral into products to suit different investors and customers, which broadens the appeal and reach of what we can do. And to the extent we continue to innovate on the liability side, it will need to be supported on the asset side.

■ **TAPLEY** It is similar for ANZ in that the challenge is around the asset base. It is an amortising book and a very competitive loan market, particularly in institutional and corporate lending. With interest rates going down, there is a lot of refinancing so managing the portfolio can be quite challenging. GSS bonds will continue to be part of the annual funding strategy for ANZ – there is certainly no shortage of desire.

■ **JENKINS** National Australia Bank (NAB) had an active year in 2018, with four different GSS transactions across US dollars, euros and Australian dollars. This took more than A$2 billion of assets out of our eligible collateral pool.

There is certainly no shortage of demand – we are asked by investors all the time whether we are doing more. We would love to do more so we are looking at all possible opportunities.

For example, NAB is a big agriculture bank so we are looking into opportunities in agriculture and forestry. Renewable energy is extremely competitively banked so our balance-sheet growth has been constrained in this space. There is capital recycling, too, so loans are being refinanced and we are bringing on new ones.

When we look at bond issuance, our preference is to issue benchmark deals. Our first Australian dollar deal was A$300 million and next time we issue a GSS bond in Australia we would like to have another benchmark-sized transaction. We also have the potential to issue more social bonds and we are working on this too. I think 2020 will be an active year for NAB.

■ **MITCHELL** At the outset of setting up these programmes and putting together NAB's frameworks for green and social bonds, we were more than happy to do bespoke, niche offerings to get the market started and demonstrate capacity.

But we have reached a point of greater maturity in the market globally so we are now focused on benchmark offerings that fit in as a regular part of our funding toolbox.

"IF WE COULD ISSUE A$2 BILLION OF GSS BONDS EVERY YEAR, WE ABSOLUTELY WOULD. BOND ISSUANCE IS A GREAT DEMONSTRATION OF WHAT THE BANK IS DOING IN THE GSS SPACE AND ALSO DEMONSTRATES OUR CREDENTIALS TO INVESTORS GLOBALLY."

SCOTT MITCHELL NATIONAL AUSTRALIA BANK

issuance from offshore corporates and financial institutions, which is good for the expansion and liquidity of the market.

Another positive theme on the corporate side is that the domestic market is the option of choice at the moment. This has not always been the case but I don't see it changing in the immediate future. Then it is a case of whether or not the issuer has the bandwidth to look at a green or sustainability deal.

■ **TAPLEY** What is also pleasing is that there has been repeat issuance. New South Wales Treasury Corporation (TCorp) and Bank Australia have come back while NHFIC is the first issuer to do two social bond deals in one calendar year. In New Zealand, Kāinga Ora – Homes and Communities, Argosy Property and Auckland Council have all returned to the GSS bond market, while Contact Energy also issued its first green bond during 2019. This speaks to confidence from borrowers that they have their frameworks and their asset bases in place. It also speaks to confidence and appetite from investors.

Swiss Why have there not been as many Australian bank issuers in the domestic GSS market in 2019?

■ **MITCHELL** We have issued GSS bonds in Australian dollars, US dollars and euros. GSS bonds are sought after in our local market and there is certainly appetite but it is not necessarily accretive to our total investor universe. This is probably why there hasn't been the volume or breadth of issuance from financial institutions in Australian dollars – compared with euros, where there are far more specific and granular mandates in the GSS space.

We want to have as many avenues available for diversification as possible. In this sense, Europe has led the way for issuance in GSS format, as it is accretive to our total universe and expands our investor base.

Australia is very much on the journey towards this being the case, but it is behind Europe. It will probably evolve in time and we will potentially see some bifurcation in demand for GSS products and traditional vanilla bonds.

INTO THE MAINSTREAM

Zaunmayr We have heard from banks in Europe that an emphasis on sustainable lending helps incentivise and focus the minds of people within a bank on ESG lending, and thus helps drive the bank's own sustainability strategy. Do you agree there is a virtuous circle here?

MITCHELL To be able to issue thematic GSS bonds, issuers need to have a strategy directed towards green lending and socially responsible objectives. In our case these align with the UN Sustainable Development Goals. This comes first and foremost.

The benefit of having a strategy and appetite for this type of lending is that, as funders, we can apply this collateral to the issuance function and feed the appetite for GSS product in debt capital markets.

Another benefit of a clear sustainability strategy for organisations relates to the way investors that are allocating capital to us view and score us as an issuer. Having clear and articulated sustainability strategies and providing a demonstration of how we are addressing climate change are becoming increasingly important. This is about issuance not only in GSS formats but across the whole spectrum of products.

CHEN I agree that there is now better integration of ESG from investors. Increasingly, they are looking through the asset pool and are interested in the broader ESG strategy and performance of borrowers because they can affect the underlying credit.

Swiss Are investors asking more questions on ESG even outside the context of GSS bond marketing?

MITCHELL Certainly. We see insurance companies, fund managers, pension funds and others on roadshows and they all have stakeholders that are demanding a better appreciation of what impact is being made from where they are investing their money.

Increasingly, investors want a better understanding of what their capital is going towards and whether it fits with their own sustainability principles. It is more important than ever to have a well-formulated and understood policy on sustainability.

Zaunmayr To what extent do the future prospects of the use-of-proceeds market in Australia rest on the growth of 'dark-green' investment funds – on the basis that without significant incremental liquidity there isn't really much purpose for issuers to engage with the product?

JENKINS I think we often get caught up in definitions of dark- and light-green investors. This is a challenge because the market has evolved so rapidly in recent times. In the early days, the main rationale for doing a GSS deal was investor diversity and targeting specifically dark-green investors. For example, World Bank will issue in GSS format only if there are incremental dark-green investors it can access.

We have moved beyond this, though – certainly for bank and semi-government issuers. The Australian market is following what has evolved in Europe, where there are familiar investors that buy GSS debt and manage large pools of capital, either across multiple strategies or in bespoke sustainable funds for customers.

Some familiar names – like Altius, AMP, Pendal, Pimco and UBS Global Asset Management – are arguably dark green because they have dedicated sustainable funds. It is still possible to classify these and many other large investors as both light and dark green – either or both.

If they are managing funds that integrate ESG screens first but don't run specific sustainability strategies or funds, we consider them light green. Investors that are signatories to the UN Principles for Responsible Investment (PRI) manage funds that need to be deployed in this way but don't

"As we get more sector definitions – beyond renewable energy, buildings and low-carbon transport – there will be more definitions of green and social. This will open up the market to more potential issuers."

MICHAEL CHEN WESTPAC BANKING CORPORATION

GREENING *TIER-TWO*

In September 2019, ANZ Banking Group (ANZ) returned to its issuance of UN Sustainable Development Goals (SDG)-linked bonds with a euro tier-two deal. There is also a bid for subordinated labelled deals in Australian dollars, as evidenced by Mitsubishi UFJ Financial Group (MUFG)'s green tier-two bond priced the same month.

ZAUNMAYR ANZ chose the euro market for its return to SDG bond issuance. As this jurisdiction is the most developed global market for GSS bonds, might we see the banks focus their issuance efforts in Europe in future?

■ **TAPLEY** The main consideration for the euro transaction from a sustainability perspective is the sophistication of the investor base. European investors understand our framework. We are speaking to assets that fit a selection of the SDGs and Europe is where we understand there to be the most sophistication around understanding what this means.

■ **WHITE** It is clearly the broadest market for diversification. We had two teams in Europe for a week and touched more than 100 investors during the roadshow. The deal was the first tier-two SDG bond from a major bank, which added to its appeal.

There is typically a big focus from offshore investors on Australian property valuations and exposure. However, on the recent ANZ roadshow, there were minimal questions on property – which is testament to investors' focus of on the ESG elements of the transaction.

ZAUNMAYR When Mitsubishi UFJ Financial Group (MUFG) issued its Australian dollar green bond, the issuer said the GSS space was a good way to find incremental liquidity for its total loss-absorbing capacity (TLAC) requirement and added it was keeping suitable assets in reserve for TLAC deals. Do other banks see the GSS space as a good way to find tier-two liquidity?

■ **MITCHELL** It is interesting that ANZ chose to issue a tier-two bond with a GSS overlay. A handful of issuers in Europe have looked at doing this, but it is not something investors should expect from NAB in the near term.

If there is broad acceptance and investors have an appetite for GSS tier-two, it would be incumbent upon us to feed that appetite. However, capital is a reasonably distinct asset class and I am not sure we would see the benefit of the accretive or targeted demand we are looking for when it comes to GSS issuance.

■ **WHITE** MUFG's deal was well received and there was incremental demand from investors in Australia and offshore. The domestic market is untested for a tier-two green bond but the trend has been that these products increase investor diversity in the Australian dollar market.

There is no reason why the domestic market couldn't be considered for this type of issuance and I think it would be well received. The ANZ euro SDG tier-two deal certainly attracted incremental demand.

■ **JENKINS** The most recent deals that have come to the domestic market show the continued growth of the investor bid. New South Wales Treasury Corporation had more new investors, bigger ticket sizes and more diversity in its sustainability bond deal. We were all surprised on the upside, again, with the size and the scale of demand.

The same can be said for MUFG. Compared with some of the Japanese banks that came earlier in the year, you could say there was a different set of investors in the pool.

MUFG was focused on the incremental bids and cost. It is no secret that the deals need to be cost-competitive relative to offshore markets. It was certainly the case in this deal. This can't be guaranteed from the outset: you need to have conviction. MUFG did but it was not an easy journey to get there.

"THE DOMESTIC MARKET IS UNTESTED FOR A TIER-TWO GREEN BOND BUT THE TREND HAS BEEN THAT THESE PRODUCTS DO INCREASE INVESTOR DIVERSITY IN THE AUSTRALIAN DOLLAR MARKET."

PAUL WHITE ANZ

have dedicated standalone green funds would also fit into this light-green category.

Whenever deal statistics come out, the breakdown of dark versus light green is often contentious. Members of the same syndicate often have different categorisations. Unless you tease out specifically which mandate an investment is going to, you are reliant on judgement calls to assess the dark- and light-green split for each deal. Often there is just categorisation as either green or nongreen. Green being those that are considered light or dark green, are signatories to the PRI, have ESG integration in place and manage funds across either or both standard and sustainable mandates. Nongreen would be those that buy purely for liquidity or because they like the credit, irrespective of the nature of the deal and issuer.

Swiss Is a move away from strict definitions an example of ESG becoming more mainstream?

TAPLEY Definitely. The corporate world is understanding, from C-suite down, that sustainability needs to be core to strategy. It needs to be high on lists of key material risks to be assessed and addressed. It is the same for investors. If they do not understand that ESG is a core part of their strategy as a portfolio manager, in time they will be out of business.

WHITE I agree with Katharine Tapley. Every investor we speak with has its own ESG screening and scoring. It doesn't matter whether it is a specific green investor.

CHEN I agree. Our discussions with investors when they assess GSS bond issuance include the overall ESG performance of the borrower. Some borrowers want to come to market with a GSS transaction straight away and we advise them that they need to have a broader sustainability strategy across the business, because investors care about this. They look at ESG as part of the broader credit profile.

Some European investors have even begun to divest names because of their exposure to carbon-intensive industries. It is front and centre – and not just with dark-green investors.

Swiss What are the main initiatives underway to push forward in sustainable debt markets?

TAPLEY A few things are propelling the market forward, such as the Australian Sustainable Finance Initiative (ASFI) (see p34). This is a cross-sectoral initiative aimed at making recommendations on how the financial system needs to change.

Regulators have also been vocal and clear on where they believe the financial-services sector needs to be. This sends a clear signal to anyone who borrows or needs insurance. The Task Force on Climate Related Disclosures (TCFD) is another example – it is a tool to enact the Australian Prudential Regulation Authority (APRA)'s messaging, which is that climate-change risk is a financial risk.

JENKINS APRA has reiterated its position a number of times. The Australian Securities and Investments Commission has also made statements relating to ESG and climate risk disclosure under TCFD reporting. And, at the end of 2018, the Australian Accounting Standards Board provided guidance around climate-related and other emerging risk disclosures which should be considered and included within financial statements.

The push for increased transparency and disclosure is continuing as a theme. Investors expect it. When we take issuers on GSS deal roadshows, they are expected to disclose what specific impact reporting will be provided for each deal. This is different even from a couple of years ago.

Swiss A lot of the guidance from regulators has been suggestive rather than prescriptive. Would more concrete regulation help drive the market forward?

JENKINS It may provide the market with more certainty. In New Zealand, for instance, the government is consulting on a proposal to make TCFD reporting mandatory.

Most large, listed corporates and financial institutions already report under TCFD or are working towards doing so. This reporting is voluntary, but if you are not doing it investors may ask why. It is all part of being more transparent and assessing risks.

In Australia, we have transition risk because of the nature of our energy, industries, resources and manufacturing sectors, which all tend to be emissions intensive. However, detailed transition plans are in place for many companies.

For example, BHP Billiton has a plan to exit fossil fuels and is looking at a range of other transition measures. Transition financing through loans linked to this transition, or use-of-proceeds bonds that fund transition investments, would make sense for a company like this.

This is where we get back to a definitional challenge, though. If a transition bond is structured as a use-of-proceeds transaction, it will be different from some of the structures we see for general corporate proceeds or for sustainability-linked products. Transition is a broadly defined and evolving term.

Zaunmayr How far away might the Australian market be from seeing the issuance of a transition bond or a sustainability-linked bond?

TAPLEY I think we will see sustainability-linked bonds in the Australian market within the next 12 months.

JENKINS The question is how big, how liquid and how frequent sustainability-linked bonds will be. We would not want them to become very niche and done only once. There are challenges to creating large, liquid transactions of this sort because by their very nature the deals are bespoke and having transparent pricing and providing secondary markets is challenging for such structured products.

In much the same way that the GSS market started with simple use-of-proceeds structures and has taken several years to get where it is now, there is considerable development to come in this space.

Swiss How do you encourage investors to change the way they view these products in order to push the market forward?

TAPLEY Ongoing dialogue is the key. It can help if you find a transaction where you can use a couple of investors to cornerstone.

JENKINS Investors want to see measurable impact with financial outcomes. In all honesty, I think a use-of-proceeds transaction makes more sense initially. A coupon linked to sustainability outcomes is quite niche and it will take time to find sufficient issuers and investors willing to participate and create a liquid market for these types of bonds.

The market has evolved from sustainability bonds placed within use-of-proceeds transactions to behavioural-based SLLs. But it took a while to get from one point to the other. It will also take time to get to a sustainability-linked bond market with coupons that step up or down. We have had structured instruments linked to ESG outcomes, but not yet with significant scale.

Swiss Why is it important to encourage investors to look at transition products?

TAPLEY Because they would be meaningfully accelerating transition if they did so.

DEAN I think developing transition bonds is very important for the GSS bond market because it would broaden the scope, especially in Australia.

It may kick off in the loan market, and one of the things we have talked about is a green loan linked to asset financing. This could provide a starting point. It would be a light-green loan, for example to a company that collects waste and wants to convert its truck fleet to the use of gas fuel.

CHEN Transition products have a lot of potential in Australia, given the make-up of the industries here. Until recently, many investors and stakeholders were only comfortable with assets that were dark green. But this could hurt the broader economic transition that is required and may also limit the efficacy of the sustainable-finance market. My view is that we need to be less purist and develop different shades of green.

The transition story is pertinent to Australia, and other markets such as New Zealand and Canada, where there are large, emissions-intensive industries. Definitions relating to transition are being debated at the moment but nothing has been set or agreed upon. There will be a lot of discussion on this over the next 24 months, which I think is needed.

JENKINS By their nature, the sectors where transition bonds would be relevant are the hardest to abate so the question is where investors can have the most impact. These companies might not be making significant green investments with the underlying assets they are financing, but they may well be making more material impact if they have committed to transition towards more sustainable and low-carbon businesses.

Several airlines, for example, have made commitments to transition to carbon neutrality, which has big implications for their businesses. How they finance this transition is important. AGL Energy (AGL) is another good example. It could earmark some of its renewable assets and issue a green bond or, alternatively, the company could do a corporate-level transition bond linked to its sustainability ambitions, including alignment with the Paris Agreement goals.

TAPLEY AGL's SLL was linked to increasing renewables capacity and reducing emissions intensity. This was in line with the sustainability targets it already had in place, which sit within the tenor of the loan. There was also a two-way pricing grid so there will be consequences if progress doesn't happen within the life of the loan.

JENKINS The unique thing about what AGL has done is disclose these metrics. It is an annual step up or down and the company has been transparent. It is all in the public domain.

WHOLE-OF-BANK APPROACH

Zaunmayr In the absence of favourable capital treatment, how easy is it to create internal incentives for products such as SLLs?

CHEN First and foremost, the main incentive for us is to partner with our customers to become more sustainable. Then, as it relates to capital treatment – whether regulated or via internal adjustments – the response needs to be measured. We are having a lot of internal and external conversations around this. My personal view is that capital weighting should be entirely risk-based. No-one should want to rush something through and be left with a question of who pays at the end. Therefore, we need to get much better at quantifying ESG factors. This will help with allocating capital weightings in the right way.

MITCHELL The European taxonomy is where the rubber hits the road with economics for a lot of this. Capital incentives or a taxonomy would likely push into the next phase of maturity for the format. If we really want to continue to see the breadth of sustainable finance evolve and expand, eventually economics will play a part. This would provide incentives for the allocation of finite resources and capital to this type of lending and the pricing transmission mechanism would also become clearer.

Ultimately, there is appetite that stems from the top of the business and then there is the economics, which is the transmission mechanism through things like capital benefits and charges to incentivise growth. This could really propel things forward on a sharper trajectory. What form this takes and under what timeframe remain unclear.

TAPLEY For ANZ, it is more about overall strategy. It starts and ends with our purpose. Our chief executive, Shayne Elliott, made a statement around the time of our annual review, published in November 2019, which reiterated that ESG is now part of everything we do.

Because sustainability is business-as-usual, the need to create specific incentives to create specific types of deals does not really exist – it is just how we operate. Frankly, customer demand is so great that if as a bank you are facing a customer and do not have the capability or willingness to engage in the sustainability conversation, customers will go next door. This is incentive enough.

JENKINS It is similar for NAB. Five or six years ago, working on green bonds often felt like a slower process.

We have similar conversations with issuers. What TCorp is doing internally regarding sustainability is helping shape what the broader market is doing. At NAB, the sustainable-finance team plays a key role in informing and shaping strategy, which is extremely interlinked with what we are doing across the broader bank.

We are increasing our commitments to deploy capital towards environmental- and sustainability-themed financing. We have recently announced our coal-financing strategy, with targets in place to get there.

However, we don't just leave these customers behind: we support their transition. For customers looking to transition, sustainable financing is the perfect opportunity. Customer discussions are now more around what can we do and how can we do it rather than just describing sustainable finance.

Much of what we do is education. We bring customers along for the journey. We have had the benefit of being at the front line for a while now, facing investors' expectations and being at the forefront of market development. We often hear from issuers that have done roadshows offshore that they have been asked ESG-related questions for which they were unprepared. It is a collaborative approach whereby we can show our clients how we are approaching ESG and sustainability as an issuer, as a corporate and as a bank financier – and why it is important to us.

Zaunmayr Natixis recently visited Australia to spread the word on work it has done to understand the climate-related impact of its whole balance sheet. Would such an approach be conceivable in Australia – and would it have value?

TAPLEY I admire what Natixis has done. It is phenomenal and market-leading. This move will be a huge competitive advantage for Natixis, at least with regard to what is expected from the regulators in Europe. It would be a competitive advantage for the Australian domestic banks to be looking at this, too.

We have met with Natixis and also started conversations internally around what we could be doing to assess the risk in our balance sheet beyond what we do on a qualitative basis as part of our usual credit assessment of customers. This is about taking it to quantitative from qualitative.

JENKINS Natixis presented to a broad segment of the team at NAB while in Australia, from risk partners to the balance-sheet, treasury and sustainability teams.

The best thing is that Natixis is happy to share its experience. There is intellectual property involved but collaboration is at the forefront. We each have bespoke systems and challenges around technology as well as resource constraints. We would love to be able to push this to the front of the priority queue but other challenges also demand financial and technology resources.

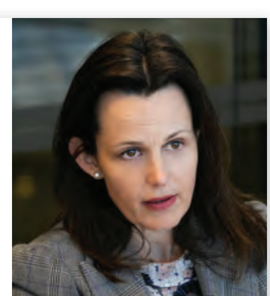
DEAN The key question with what Natixis has done is where its cost of capital goes as it transitions to a greener balance sheet. This is an interesting question for banks to consider.

We are looking internally at potentially putting in place a similar mechanism. It would not be as detailed as what Natixis has done, as this would be difficult for an Australian bank.

Our strategy would involve adjusting the internal capital charge for deals that meet certain criteria, to encourage more of it. This could be done formally through internal structures or informally through pricing matrices.

"The corporate world is understanding, from C-suite down, that sustainability needs to be core to strategy. It needs to be high on lists of key material risks to be assessed and addressed. It is the same for investors."

KATHARINE TAPLEY ANZ



WHO GAINS FROM *BAD PERFORMANCE*?

One of the more interesting anomalies of sustainability-linked securities is that investors can benefit, in the form of margin step-ups, from a borrower's poor sustainability performance. The market is still discussing the most appropriate response.

SWISS There is a moral issue around what investors should do with the gain made from an issuer missing its targets in a sustainability-linked loan (SLL) or sustainability-linked bond. How is this being addressed?

■ **JENKINS** I know investors that are already thinking this through in the context of sustainability-linked bonds and how to manage this should it occur. Some European borrowers have already entered into SLLs where they have stated that if they were to get a coupon step-down they would want to reinvest it into other sustainability-linked measures.

We advocate that SLLs have both margin incentives and penalties to encourage ambitious and material environmental, social and governance (ESG) risk and sustainability improvements from borrowers. This should improve ESG risk and, in the longer term, credit risk.

■ **CHEN** It is a tricky issue but I still advocate for both a step-up and a step-down. At the moment, it is a bit of an incentive for the client but, down the track, SLLs should have KPIs that more explicitly affect the underlying credit profile of the borrower. If you follow this logic through, you need the step-up and step-down.

Philosophically, I have no issues with investors accepting a higher margin if ESG performance drops, because this reflects underlying credit performance. But optically, there are challenges to this, so I like the idea of reinvesting incremental returns.

When we talk to clients, we are always pitching to have both step-up and step-down provisions. This is how you get credibility, as both parties have skin in the game. For ESG-linked bonds, there is nothing that stops the structure of a step-up and step-down being used, it is just whether investors are willing to take a step-down.

■ **DEAN** It shouldn't be too easy for issuers. Sometimes issuers say it is too complicated, but the structure needs to hold them to account. It can be tailored, but for issuers to get the credit, the product needs to have credible targets.

This is our approach, instead of having a target of lending a certain volume of SLLs by a certain date. We are not in the business of growing this product just for the sake of it. Similarly, I have no interest in doing a deal with a borrower that just wants the discount.

SWISS How important do you think the education piece is for issuers?

■ **CHEN** It is still important, not least because we would question deals with borrowers that are just in it for a discount. I think it also helps with market development.

There is an example with the green-bond market. It boomed initially, and then there were many questions around greenwashing. Now we have definitions and standards in place to help with legitimacy.

It will likely be the same with SLLs. We may be in a honeymoon period at the moment. But if deals are structured just for cheap financing and the targets aren't based on material issues or aren't incremental, it could impede the development of the market.

"WE ADVOCATE THAT SLLs SHOULD HAVE BOTH MARGIN INCENTIVES AND PENALTIES TO ENCOURAGE AMBITIOUS AND MATERIAL ESG RISK AND SUSTAINABILITY IMPROVEMENTS FROM BORROWERS. THIS SHOULD IMPROVE ESG RISK AND ULTIMATELY CREDIT RISK IN THE LONGER TERM."

DAVID JENKINS NATIONAL AUSTRALIA BANK

The big question is whether governments will come to the party with capital relief. We understand there have been discussions with the Chinese regulator and there have certainly been conversations with the European regulator. It would be a game changer if major economies had this kind of regulatory capital adjustment for green lending. But we are not waiting for it.

■ **JENKINS** For NAB, ESG is part of the credit-risk assessment process in every transaction we do. For Natixis, it is a net-zero game where some win and some lose.

The conversation is changing. For example, a few years ago, when asset-backed securities featuring solar photovoltaic technology were a new asset class, the focus may have been track record for the asset class. This is still relatively pioneering but there are now data sets that show outperformance of entities that have good ESG ratings.

Swiss Australia doesn't seem to have much political impetus to support sustainable finance. Despite this, the local market is quite developed compared with parts of the world like the US and Asia. Is it enough for the market to drive development or would you like to see more political support?

DEAN It is our clients that drive it. In renewable energy, if we had waited for government regulation the market would not have developed as much as it has. Given the influence of Westpac Banking Corporation (Westpac) and the other major banks in financing greenfield development, waiting for regulation would have held this back.

Now, the scale of development in renewable energy is helping the Australian government meet its targets.

MARKET OUTLOOK

Zaunmayr What do participants believe will be the biggest developments in the sustainable-debt market, globally and in Australia, in 2020?

MITCHELL It will become incumbent on issuers of significant volume into debt capital markets to have pathways and strategies on their sustainability agendas that are better articulated and understood.

Global investors now generally expect us not just to have a programme for issuing in GSS format but a top-down, overarching strategy, over the whole bank, to get investors engaged with NAB rather than just with specific products. It is becoming more about integrated assessment.

JENKINS We will see more sectors and more formats, but also more synthetic and capital-release transactions. The French banks have led the charge with capital-release transactions, which free up capital to be deployed towards positive impact and sustainable finance. This aims to free capital from legacy transactions for lending that delivers more positive, sustainable and impactful outcomes across industries.

We will also see securitisation in different formats, given the scale of issuance. There will also be finance linked to sustainability and transition in a range of formats and catering to different customer segments.

TAPLEY Away specifically from product, I think disclosure and TCFD will pick up momentum in 2020. We are moving towards this becoming compulsory and certainly there are not many customers we are talking to that are not looking at disclosure and how TCFD fits in to provide more transparency.

WHITE We will see more sustainability-linked bonds, particularly in Europe. We have also seen product innovation in derivatives and I am sure this will continue. There are a lot more private placements for longer-tenor deals happening in Asia. Given where rates and yields are, we expect this to continue. There could also be more targeted, investor-led themed transactions over time.

CHEN A few interesting things have developed over the last 12 months that could set the stage for future development. Labelled product can trickle to other instruments. Towards the end of 2018, Westpac launched the world's first certified wholesale green deposit product. For any product now, there is the question of whether a sustainability lens can be applied to it. This could be for trade finance, for example.

We said at this discussion at the end of 2018 that SLLs were the main expectation for development in 2019 and we have been proved right. I think there will be exponential growth in this product over the next 12 months.

Earlier in this discussion we also touched on the transition issue. I think this will come to the fore over the next 12 months. I don't think we will land on a set of agreed-upon definitions as yet, but Australia is in the driver's seat for what transition looks like.

DEAN I agree. I think this is the evolution we will start to see. It's not that there will be one product fully developed and mature before something else comes from it. The evolution into transition financing will get going over the next year.

It is also not just loans and bonds. I think we will continue to see sustainability raised in other areas, like asset finance. This expansion will make sustainability much more mainstream than just having loans and bonds. The SLL area is the logical place for borrowers to start but it is not necessarily what we are targeting.

For Westpac, I would like to see the whole product suite develop so it becomes mainstream and borrowers think about financing in a sustainable way.

If you think about corporate structures, treasury teams look at loans and bonds, someone else looks at trade finance and someone else does asset finance. Mainstreaming sustainable finance means different people in our client set start to think about their requirements from financiers in a way that broadens the sustainability financing platform.

JENKINS There should be more growth in the retail sector, with products targeted specifically at these investors. There is a focus globally on green mortgages, which is a particularly large growth opportunity for Australia given the nature of our housing stock. Exchange-traded funds are another area that is easy to access for retail investors and is growing quickly.

We would like to raise more green deposits. We need to look at what is the better outcome for our customers and the community.

TAPLEY Away from capital markets, the lending market should continue to flourish. It is interesting to observe what has been happening with SLLs in Australia, in that they have tended to facilitate the return to the syndicated market of borrowers that had otherwise been doing bilateral deals.

They have been bringing their bilateral facilities together into a sustainability-linked format, which is then taken to the syndicated market. This is interesting from a structural perspective.

JENKINS The loan market is seeing more participants interested in deploying capital to support sustainability so it is likely that it won't continue to be just the banks in this space. The banks have taken the lead but long-term investors that want to invest in loans and have an ESG focus will be keen.

There will also be opportunity for the banks to recycle some of the lending they do internally as it gets to scale. There could be bonds or asset-backed transactions linked to this lending. •

Becoming guardians of a sustainable world

A year after it was established, the **New Zealand Sustainable Finance Forum** (NZSFF) published an interim report and legal opinion on how the country can shift to a more sustainable footing. NZSFF co-chairs, **Karen Silk**, general manager at Westpac in Auckland, and **Matt Whineray**, chief executive at New Zealand Super Fund in Auckland, provide an exclusive overview of this work.

"He waka eke noa"
(We are all in this canoe together)
MĀORI PROVERB

The NZSFF was launched in October 2018, tasked with designing a roadmap to help the country shift to a financial system that supports economic, social and environmental outcomes that align with New Zealand's commitments under the Paris Agreement and UN Sustainable Development Goals (SDGs). The NZSFF is the first project launched by the Aotearoa Circle – a unique partnership of public- and private-sector leaders committed to the pursuit of sustainable prosperity and reversing the decline of New Zealand's natural resources.

The forum's interim report, pubished in October 2019, reviewed the latest international thinking and best practice to produce a a 'future state' vision for New Zealand's financial system.

It assesses how well the prevailing financial system is performing against this benchmark and poses some initial ideas on questions relating to potential pathways for change.

The NZSFF has invited feedback to February 2020, after which the report will be finalised and a roadmap for action on how to shift New Zealand to a sustainable financial system will be drawn up, planned by the end of July 2020. The NZSFF intends that the roadmap will include specific recommendations on reshaping the current financial policy, regulatory and market framework.

Update from NZSFF co-chairs

New Zealand's indigenous Māori people see our place it the world in terms of *Kaitiakitanga*, which roughly translates to guardianship. It is a concept that fits nicely with our understanding of sustainable finance and has guided our work of building a stronger economy.

The NZSFF has been established to set up the framework for our country's financial system, so it supports the transition to a low-emissions, resilient, resource-efficient, just and inclusive economy.

We believe everyone in the investment community should see themselves as guardians, or *kaitiaki* – because the choices we make about where to allocate capital and how to price risk underpin how the global economy operates.

This means we have direct influence over the wellbeing of people and the planet. Long-term societal trends have an impact on financial outcomes – this is the *impact on business* – and lending, investment and insurance decisions also have an

"WE NEED TO SYSTEMATICALLY ALIGN NEW ZEALAND'S FINANCIAL SYSTEM WITH THE TASK OF MEETING OUR 21ST CENTURY SUSTAINABILITY CHALLENGES, AND IN THE PROCESS PRODUCE BETTER OUTCOMES FOR ALL NEW ZEALANDERS."

KAREN SILK

impact on long-term societal trends – this is the *impact of business*.

The NZSFF has named leadership, improving the availability and quality of environmental and social data, and pricing natural and social capital as its three top priorities. One key goal is to see what economists call 'negative externalities', whether they be the impact on the climate, the loss of biodiversity or the impact on people of unjust labour practices, properly priced into the market.

“THE IMPERATIVE FOR BUSINESS AND THE FINANCIAL SYSTEM IS CLEAR: A STRONG ECONOMY DEPENDS ON A HEALTHY SOCIETY AND A CLEAN ENVIRONMENT. THESE ELEMENTS CAN NO LONGER BE SEPARATED FROM EACH OTHER AND NEED TO BE ACCOUNTED FOR IN THE SYSTEM.”

MATT WHINERAY

In the course of consultation for the interim report, we heard that Māori do not think in terms of negative externalities – nothing is external to the system. Rather, everything is interconnected. It is the understanding that you cannot divorce the actions of business or investment decisions from the wider world, because practically you either do damage to the whole system or eventually your actions will catch up with you and the consumer, regulator or competitor response will overwhelm you.

Having accurate and comparable data is a key element in valuing assets and investments. However, environmental and social data needs improved accuracy, comparability and availability to become integral to financial decision-making. Currently, the global financial system is built on models, norms and rules that do not reflect the full cost of business or respond to changing societal expectations.

We believe integrating environmental and social impacts will improve the accuracy of valuations, accounting and capital-adequacy models, and internalise social and environmental costs. Doing so will create a system that is more stable, sustainable and resilient. It also aligns capital with the long-term wellbeing needs of society, the environment and the real economy. It will prevent the misallocation of capital to activities that use natural capital but don't bear the cost of that usage.

As part of its work, the NZSFF produced an independent legal opinion. This says climate change has moved from being recognised solely as an environmental issue, to a discrete – and foreseeable – financial risk to business. The foreseeable consequences of climate change, arising both from direct physical impacts and the second-order effects of transitioning to a low-carbon economy, should be managed by directors and investment professionals as they would any other financial risk.

The opinion also states that fund managers, in acting in the best interests of their investors, now have a duty to take climate-change risk into account when designing investment policies, where to do otherwise could pose a material financial risk to the portfolio.

Fund managers may also need to implement a climate-change investment strategy to future-proof funds for investors. The effect we witnessed of an Australian legal opinion along similar lines on the discussions around Australian board tables was significant and we are already hearing of a similar response in New Zealand.

The change to more sustainable finance systems is taking place around the globe, and economic foundations are shifting to accommodate this change. For example, the Task Force on Climate-related Financial Disclosures (TCFD) is gaining international momentum in pushing businesses to provide more information on climate-change risk, with the UK mandating disclosure requirements for large companies and asset owners by 2022. The government is currently consulting on a proposal to make TCFD reporting mandatory in New Zealand.

In September 2019, the Principles for Responsible Banking were launched by the UN Environment Programme Finance Initiative in New York, covering 130 banks from 49 countries, with more than US$47 trillion in assets. The principles intend to align banks' strategies with society's goals as expressed by the SDGs and the Paris Agreement.

The EU is introducing stronger reporting requirements regarding sustainable finance with a strong focus on taxonomy, while the Australian Prudential Regulation Authority has stated that climate risk is foreseeable, material and actionable. In New Zealand we have legislated a target of producing net zero carbon emissions by 2050, while enironmental, social and governance reporting was recently incorporated into our stock exchange's corporate-governance code.

Asset owners, investors and businesses should become the guardians of these changes. Building a more sustainable finance system will improve decision-making, better allocate capital to productive uses, increase transparency and facilitate the long-term wellbeing of society. It is not just the right thing to do. It also makes economic sense. •

A market takes shape

New Zealand's green, social and sustainability (GSS) bond market grew substantially in 2019 but is still concentrated around a few repeat issuers. At the **KangaNews-Westpac New Zealand Sustainable Finance Summit** in Auckland in November 2019, market participants discussed developments in the GSS market and the wider application of sustainability.

JOANNA SILVER WESTPAC

It would be fair to say that 2019 has been a tremendous stepping stone and potentially a tipping point for civil society, government and business on sustainability and the broader need for horizons, investment considerations and business strategies to change.

JOHN DUNCAN INDEPENDENT DIRECTOR

I think it's important to take a tactical approach when a company is in the earlier stages of engaging with sustainability, rather than trying to solve everything in one go. That gets too hard for management, and it's more important to get things moving and embed programmes in an organisation for the long haul – long after the current directors have gone.

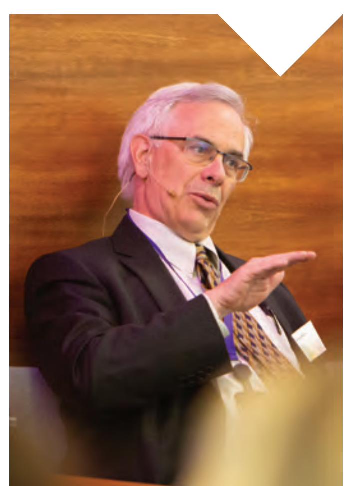
JULIA HOARE INDEPENDENT DIRECTOR

When a large ship starts to turn, the flotilla around it has to turn, too. I view Watercare's sustainability commitments a bit like this. We have a huge number of suppliers and we have to think carefully about what our commitments mean to them. We have spent a lot of time working on our supplier code of conduct – working out how those ships can turn with us and not sink.

JONATHAN MASON INDEPENDENT DIRECTOR

As a director, if you don't think a company you are invested in is pushing aggressively enough on sustainability you should ask for a report on sustainability and put it on the 'matters arising' schedule. If something is on that schedule, it tends to get done.

Sustainability is now sufficiently important that I want to see a five-year sustainability strategy from every company for which I'm on the board. Companies are at different stages of maturity on this, though. You have to work with them according to where they are.



CRAIG STOBO INDEPENDENT DIRECTOR

Shareholders should be asking us as directors how aligned our businesses are with the horizons that ESG challenges present. As guardians, we ought to embed horizons into our planning – and I'm not sure how well we are doing so.

DAVID BENATTAR
WAREHOUSE GROUP

We have to justify investments, even sustainability ones – and this means having a framework in place for reporting on their value. We used integrated financial reporting for the first time this year, and I think it is our job as a business to tell the story on the value of sustainability to our shareholders.

MIKE ROAN MERIDIAN ENERGY

Building up reporting frameworks may sound boring, but it allows a corporate culture to grab hold of real factors. We started with two of the UN SDGs where our business could make a difference and focused our board conversation around specific areas where we could contribute to these factors.

PHIL NEUTZE AUCKLAND INTERNATIONAL AIRPORT

When we meet investors around annual results, we might get one or two questions a day on ESG concerns – in a schedule that covers 50-60 investors over two or three days. We encourage these questions and they are increasing in number, including around our community support and employment activities, diversity, remuneration and CO_2 reduction targets. But it is off quite a low base.

NICK KYNOCH FINANCIAL MARKETS AUTHORITY

We are responsible for promoting fair, efficient and transparent financial markets in New Zealand, and the same objectives apply equally in the ESG space. We want to ensure that, on the sell side, products do what they say with transparency and, on the buy side, that fund managers are true to the mandates or investment philosophies they are offering.

KATE BEDDOE VECTOR

We have been having detailed conversations with our board about sustainability for at least the last three years. This includes a lot of work around global megatrends and how they will affect our business model in the short and longer term. The environmental and social aspects of these megatrends are accelerating fast.

ROSIE MERCER PORTS OF AUCKLAND

Our sustainability strategy was born from a need to rebuild our social licence. But while the strategy came from a social goal, it quickly became clear that climate action was a big way to rebuild trust in our community.

Boards are having to be really courageous when it comes to supporting what their organisations want to achieve. We have to recognise this and, therefore, do what we can to provide boards with the right facts and figures to support the brave decisions they need to make.

We have a range of programmes around social sustainability in our business, often driven through our diversity and inclusion programme. The one I am most proud of is the living-wage accreditation, because we have also championed this throughout our supply chain. It really means something when cleaners at work tell you the extra few dollars they are earning make a real difference to their lives.

EVENT
REPORT

HAMISH MACDONALD NZX

The listed green-bond market is underdeveloped at this stage, with just three issuers and NZ$800 million outstanding. We need to enable the market to develop. We have great companies with desire to issue and there is investor demand – this is a potential competitive edge for New Zealand and we need to take advantage of it.

ABBIE REYNOLDS SUSTAINABLE BUSINESS COUNCIL

When we talk about the value drivers of sustainability, investors are among our key stakeholders. We need to understand where sustainability is emerging in the shareholder conversation.

DANIEL KALDERIMIS CHAPMAN TRIPP

Climate change is no longer an ethical consideration you can take or leave according to your politics. It is a financial consideration that applies, at least in theory, to everyone. If material, it must be taken into account.

JOHN BERRY PATHFINDER ASSET MANAGEMENT

If ESG metrics are part of an active fund manager's analysis, arguably the manager should be entitled to charge a higher fee for this service. But I'm uncomfortable with charging more for an ethical product, even if consumers are used to paying more in the real economy – like they do for an organic avocado. It doesn't feel ethical to charge more for an ethical fund.

KATIE BEITH NEW ZEALAND SUPERANNUATION FUND

There has been a recent academic study, along with two different surveys of the global investor community, on reasons for investors integrating ESG into their investment decisions. Overwhelmingly, these show that it is because of the associated risk-and-return benefits.

ROBERT MURRAY KIWI INVESTMENT MANAGEMENT

Our fundamental analysis shows a very strong correlation between companies that are well governed, have diverse boards and take social aspects seriously, and strong credit-spread performance and longevity. This is why, as we explain to our clients, we have always been rigorous in looking at these factors.

PETER JONES ANZ INVESTMENTS

In my view, the move to using the word 'sustainability' and thinking about ESG in this context moves the discussion forward. It brings a greater level of ambition to what we would like to do within our portfolios, as do the new data and metrics we can use to work out how to tackle big issues like climate change and fossil-fuel transition.

ANDREW STEEL FITCH RATINGS

The most important thing is that ESG risks don't affect all entities within a sector equally. They manifest very differently, depending on an entity's business profile, financial structure and how it reacts to the presence of a risk factor.

MIKE SANG NGĀI TAHU HOLDINGS

The financial system might not be intergenerational but our equity is – everything we put in place with our structure and investment plan is based on the concept of intergenerational equity. I don't know what is going to happen with climate change and lobster farming, say – but we have to create the capability to do this thinking within our management teams and our people.

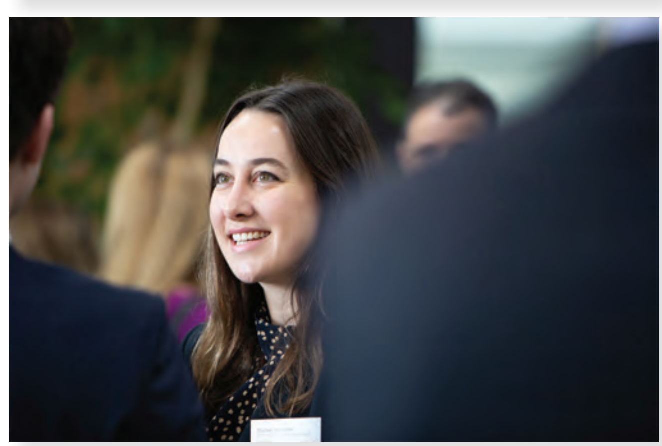
DIANA PUKETAPU
NGĀTI POROU HOLDINGS

The concept of a sustainable financial system is steeped in views of intergenerational perspectives and equity. Māori make great natural partners to participate in this. I don't mean doing the *mihi* and the cultural elements – I mean really partnering. We have to help design and deliver this financial system and become fully enabled participants in it, because the current system has plenty of inequities.

Areas such as intergenerational equity and intergenerational perspectives – things that are crucial to a conversation about sustainability – are starting to become more mainstream. But these are concepts Māori have been living with and considering forever.

JAMIE SINCLAIR NGĀTI WHĀTUA ŌRĀKEI TRUST

We spent a lot of the first half of 2019 asking hundreds of our members to tell us how they would define living well in 2050. From this, we identified eight priorities, or themes, that will drive our strategy. Number one was cultural identity. This told us that connection to culture and self-determination are very important precursors to wellbeing for Māori.



RANGIMARIE PRICE AMOKURA IWI CONSORTIA

The Māori economy is a developing economy that sits within a developed one. This poses a significant opportunity for us to flip the script, because the terrible metrics we see about Māori outcomes are a symptom of systemic failure, rather than a characteristic of us as Māori.

LIAM CLEARY WESTPAC

Coming from a jurisdiction like New Zealand, it can be difficult to find assets to meet international standards that were not set up with us in mind – like the EU taxonomy. But the market and the standards are evolving all the time.

Ultimately, we have to issue what our investors want. For domestic issuance, it is important to focus on what works in New Zealand and, wherever practicable, follow international standards.

SAM DIREEN
KĀINGA ORA – HOMES AND COMMUNITIES

It was relatively straightforward to update our programme. Wellbeing bonds are sustainability bonds with the added feature of aligning with Treasury's living-standards framework, and we thought it made sense – and sent a strong message – to re-label all our outstanding bonds.

BRYCE DAVIES IAG

As the insurance industry undergoes transition it creates its own externalities, in particular around affordability and people not being able to recover after disasters. The work we are doing is based on the idea that, while we might think we are doing a good job pricing risk and sending signals that drive change, this has real social and economic consequences.

PENNY SHEERIN CHAPMAN TRIPP

ESG disclosure is key, and there is a lot going on at the moment – including the FMA's consultation on green bonds and other responsible investment products, the government's review of KiwiSaver default providers, and the TCFD proposals. What disclosure should look like will be an important ongoing theme for our market.

KAREN SILK WESTPAC

Under the auspices of the Aotearoa Circle, we have been working on the question of how we can reshape the New Zealand financial system to do its part to preserve natural capital while continuing to direct financial capital throughout our economy.

We are a small part of the world economy but, unfortunately, we punch above our weight when it comes to greenhouse-gas emissions. To date, market short-termism, failure to price social and environmental inputs and outcomes properly, and lack of data and awareness mean capital has potentially been mispriced and misallocated.

FIONA DODDRELL WESTPAC

We have to wonder whether different regional taxonomies will make GSS products harder for investors to understand. More importantly for New Zealand, if we continue to focus on regional criteria we still need to ensure we get much-needed international capital into New Zealand.

MICHAEL SALVATICO MSCI

ESG has grown incredibly fast in the fixed-income space in the last couple of years. The investor side was growing steadily until about 18 months ago, when it just took off. As for why, I think there is more evidence around nowadays that ESG does what people have claimed it does – including helping investors identify better companies.

MATTHEW WALKER AUCKLAND COUNCIL

One of Auckland Council's largest businesses is public transport, so issuing green bonds was a simple marriage for us. We are investing hundreds of millions, if not billions, of dollars in transport infrastructure and we were able to elevate awareness of our investment plans to capital markets. It is also pretty obvious that appetite for this type of security is growing in global markets.

NIGEL GREENWOOD SYNLAIT MILK

The key differentiator with a loan that is linked to sustainability, other than being connected to our corporate purpose, is that proceeds can be applied to anything. It's not like a green bond, which has to be applied to a particular activity, but part of our standard revolving finance. It was far more flexible, efficient and effective – and we get a discount if we reach a threshold.

LOUISE TONG CONTACT ENERGY

Contact has cut greenhouse-gas emissions by nearly 60 per cent since 2012. We now have some of the most aggressive verified targets for a power company globally, which come in well below the 2-degrees scenario. Sustainability-linked loans offer an opportunity to match this type of dynamic ambition for ever-improving ESG outcomes.

ROSS PENNINGTON CHAPMAN TRIPP

If we don't get brown moving towards green we are in real trouble. Labels matter, so maybe we need to call this type of financing transition bonds rather than green bonds. But we have to have the debate, and we need all market participants to engage with it.

Deal and league tables

KangaNews is pleased to launch its green, social and sustainability (GSS) bond league tables for the Australian and New Zealand debt markets.

In setting the criteria for the league tables, consideration was given to the types of bonds that have already been issued in Australia and New Zealand, as well as to the new products issued in other jurisdictions that the Antipodean markets might take up in the future.

Most of the criteria for the league tables are the same as the criteria for the established suite of KangaNews league tables – including no minimum size, one-year minimum maturity or call date and price disclosure. What required careful consideration was how to classify a sustainable bond.

After market consultation, a decision has been taken to require the instrument to be a use-of-proceeds bond. This means sustainability-linked bonds will be excluded from these league tables if any are issued in Australia or New Zealand in the future.

Bonds that have retrospectively been labelled as sustainable bonds are also excluded. As a result, four deals issued by Kāinga Ora – Homes and Communities in New Zealand in 2018 have been excluded as they were not set up, verified or marketed as social bonds at the time of issuance.

New Zealand market GSS bond deals

PRICED 1 JAN 2014 – 31 DEC 2019

SETTLEMENT DATE	ISSUER	VOLUME (NZ$M)	MATURITY	COUPON TYPE	COUPON(%) /MGN. (BP)	BOOKRUNNER(S)	ISSUER RATING S&P	MOODY'S	FITCH
9 Aug 17	International Finance Corporation	125	9 Aug 27	Fixed	3.75	ANZ, BNZ	AAA	Aaa	
27 Jun 18	Auckland Council	200	27 Jun 23	Fixed	3.17	ANZ	AA	Aa2	
12 Jun 18	Kāinga Ora – Homes and Communities	250	12 Jun 23	Fixed	2.97	ANZ, WIB	AA+		
12 Jun 18	Kāinga Ora – Homes and Communities	250	12 Jun 25	Fixed	3.36	ANZ, WIB	AA+		
18 Oct 18	Kāinga Ora – Homes and Communities	50	12 Jun 23	Fixed	2.97	ANZ, BNZ, WIB	AA+		
18 Oct 18	Kāinga Ora – Homes and Communities	250	18 Oct 28	Fixed	3.42	ANZ, BNZ, WIB	AA+		
1 Mar 19	Contact Energy	100	15 Aug 24	Fixed	3.55	ANZ, BNZ, DC	BBB		
7 Mar 19	African Development Bank	150	7 Mar 29	Fixed	2.85	Daiwa	AAA	Aaa	
27 Mar 19	Argosy Property	100	27 Mar 26	Fixed	4.00	ANZ, BNZ, FB, FNZC			
5 Apr 19	Kāinga Ora – Homes and Communities	500	5 Oct 26	Fixed	2.247	ANZ, BNZ	AA+		
10 Jul 19	Auckland Council	150	10 Jul 25	Fixed	2.013	ANZ, BNZ	AA	Aa2	
16 Sep 19	Kāinga Ora – Homes and Communities	425	12 Jun 25	Fixed	3.36	ANZ, WIB	AA+		
16 Sep 19	Kāinga Ora – Homes and Communities	175	18 Oct 28	Fixed	3.42	ANZ, WIB	AA+		
29 Oct 19	Argosy Property	100	29 Oct 26	Fixed	2.90	ANZ, FB, HWP, Jarden			
8 Nov 19	Kāinga Ora – Homes and Communities	400	5 Oct 26	Fixed	2.247	ANZ, BNZ	AA+		

NOTE: The deals from Kāinga Ora priced in 2018 are excluded from the league tables because they were retrospectively classified as social bonds.

Cumulative New Zealand market GSS bond league tables

(INCLUDING SELF-LED DEALS)[1]
1 JAN 2017 – 31 DEC 2019

BOOKRUNNER	VOLUME NZ$M	NO. OF DEALS	% TOTAL VOLUME
ANZ	1,171	10	48.3
BNZ	646	6	26.6
Westpac Institutional Bank	300	2	12.4
Daiwa	150	1	6.2
Forsyth Barr	50	2	2.1
Deutsche Craigs	33	1	1.4
First New Zealand Capital	25	1	1.0
Hobson Wealth Partners	25	1	1.0
Jarden Securities	25	1	1.0
TOTAL	**2,425**		**100**

1. There are no self-led deals in this period.

2019 New Zealand market GSS bond league tables

(INCLUDING SELF-LED DEALS)[1]
1 JAN – 31 DEC 2019

BOOKRUNNER	VOLUME NZ$M	NO. DEALS	% TOTAL VOLUME[2]
ANZ	908	8	43.3
BNZ	583	5	27.8
Westpac Institutional Bank	300	2	14.3
Daiwa	150	1	7.1
Forsyth Barr	50	2	2.4
Deutsche Craigs	33	1	1.6
First New Zealand Capital	25	1	1.2
Hobson Wealth Partners	25	1	1.2
Jarden Securities	25	1	1.2
TOTAL	**2,100**		**100**

1. There are no self-led deals in this period.

CRITERIA FOR NZD GSS BOND LEAGUE TABLES: Must be use-of-proceeds bond; no minimum size; one-year minimum maturity or call date; dual-tranche issues counted as one deal if both tranches have the same maturity date; settlement date used for date calculations; issued in NZD; no requirements regarding domicile of issuer; pricing must be disclosed; deal must be syndicated; bookrunners given equal allocation (unless advised otherwise); excludes bonds that have been retrospectively labelled as green, social or sustainability bonds; excludes asset-backed securities.

SOURCE: KANGANEWS 31 DECEMBER 2019

Australian market GSS bond deals

PRICED 1 JAN 2014 – 31 DEC 2019

SETTLEMENT DATE	ISSUER	VOLUME (A$M)	MATURITY	COUPON TYPE	COUPON(%) /MGN.(BP)	BOOKRUNNER(S)	ISSUER RATING		
							S&P	MOODY'S	FITCH
29 Apr 14	World Bank	300	29 Apr 19	Fixed	3.50	RBC, WIB	AAA	Aaa	
16 Dec 14	National Australia Bank	300	16 Dec 21	Fixed	4.00	NAB	AA-	Aa2	
2 Apr 15	KfW Bankengruppe	600	2 Jul 20	Fixed	2.40	JPM, Nomura, RBC	AAA	Aaa	
3 Jun 15	ANZ Banking Group	600	3 Jun 20	Fixed	3.25	ANZ	AA-	Aa2	AA-
3 Jun 16	Westpac Banking Group	500	3 Jun 21	Fixed	3.10	WIB	AA-	Aa2	AA-
27 Jul 16	Treasury Corporation of Victoria	300	27 Jul 21	Fixed	1.75	NAB	AAA	Aaa	
15 Dec 16	African Development Bank	55	15 Dec 31	Fixed	3.50	NOMURA	AAA	Aaa	AAA
22 Mar 17	Queensland Treasury Corporation	750	22 Mar 24	Fixed	3.00	ANZ, BAML, NAB	AA+	Aa1	
24 Mar 17	National Australia Bank	500	24 Mar 22	Fixed	3.25	NAB		Aa2	AA-
31 Mar 17	Commonwealth Bank of Australia	450	31 Mar 22	Fixed	3.25	CB	AA-	Aa2	AA
31 Mar 17	Commonwealth Bank of Australia	200	31 Mar 22	FRN	92/BBSW	CB	AA-	Aa2	AA-
6 Apr 17	Investa	150	5 Apr 24	Fixed	4.262	ANZ	BBB+		
21 Apr 17	ICPF Finance	100	21 Apr 27	Fixed	4.25	ANZ, CB	A-		
3 Aug 17	Australian Catholic University	200	3 Aug 27	Fixed	3.70	NAB, UBS		Aa2	
3 Aug 17	European Investment Bank	200	3 Feb 28	Fixed	3.30	JPM, Nomura, TD	AAA	Aaa	AAA
8 Aug 17	KfW Bankengruppe	200	2 Jul 20	Fixed	2.40	RBC, TD	AAA	Aaa	AAA
15 Sep 17	Rentenbank	50	15 Sep 32	Fixed	3.40	DB	AAA	Aaa	AAA
28 Sep 17	European Investment Bank	125	3 Feb 28	Fixed	3.30	JPM, Nomura	AAA	Aaa	AAA
24 Oct 17	African Development Bank	30	27 Jul 27	Fixed	3.30	TD	AAA	Aaa	
25 Oct 17	KfW Bankengruppe	200	2 Jul 20	Fixed	2.40	TD, RBC	AAA	Aaa	AAA
30 Oct 17	African Development Bank	30	27 Sep 27	Fixed	3.345	JPM	AAA	Aaa	
9 Nov 17	African Development Bank	60	15 Dec 31	Fixed	3.50	Nomura	AAA	Aaa	AAA
8 Dec 17	Rentenbank	50	15 Sep 32	Fixed	3.40	DB	AAA	Aaa	AAA
12 Jan 18	European Investment Bank	750	12 Jan 23	Fixed	2.70	RBC, TD, UBS	AAA	Aaa	AAA
16 Jan 18	European Investment Bank	175	3 Feb 28	Fixed	3.30	Nomura	AAA	Aaa	AAA
5 Feb 18	European Investment Bank	400	3 Feb 28	Fixed	3.30	JPM	AAA	Aaa	AAA
12 Mar 18	European Investment Bank	200	3 Feb 28	Fixed	3.30	JPM	AAA	Aaa	AAA
15 Mar 18	International Finance Corporation	300	15 Mar 23	Fixed	2.70	ANZ, DB, Nomura	AAA	Aaa	
18 May 18	European Investment Bank	150	3 Feb 28	Fixed	3.30	Nomura	AAA	Aaa	
6 Jun 18	African Development Bank	30	27 Sep 27	Fixed	3.345	Daiwa	AAA	Aaa	
30 Aug 18	Bank Australia	125	30 Aug 21	FRN	130/BBSW	ANZ	BBB	Baa1	
5 Sep 18	Kommunalbanken Norway	450	5 Sep 23	Fixed	2.70	TD, RBC	AAA	Aaa	
7 Sep 18	Macquarie University	200	7 Sep 28	Fixed	4.50	HSBC, NAB		Aa2	
7 Sep 18	Macquarie University	50	7 Sep 43	Fixed	3.50	HSBC, NAB		Aa2	
15 Nov 18	New South Wales Treasury Corporation	1,800	15 Nov 28	Fixed	3.00	ANZ, BAML, NAB	AAA	Aaa	
26 Nov 18	World Bank	300	26 Nov 25	Fixed	2.90	CB, RBC, TD	AAA	Aaa	
17 Jan 19	Asian Development Bank	1,000	17 Jan 24	Fixed	2.45	DB, Nomura, TD	AAA	Aaa	
18 Jan 19	International Finance Corporation	400	15 Mar 23	Fixed	2.70	CB, DB, JPM	AAA	Aaa	
31 Jan 19	BNG Bank	25	31 Jul 29	Fixed	2.95	Daiwa	AAA	Aaa	AA+
28 Feb 19	BNG Bank	15	31 Jul 29	Fixed	2.95	Daiwa	AAA	Aaa	AA+
6 Mar 19	Queensland Treasury Corporation	1,250	6 Mar 29	Fixed	2.50	NAB, UBS, WIB	AA+	Aa1	
28 Mar 19	National Housing Finance and Investment Corporation	315	28 Mar 19	Fixed	2.38	ANZ, UBS	AAA		
3 Apr 19	World Bank	150	26 Nov 25	Fixed	2.90	TD	AAA	Aaa	
3 Apr 19	World Bank	50	26 Nov 25	Fixed	2.90	TD	AAA	Aaa	
16 Apr 19	Asian Development Bank	110	17 Jan 24	Fixed	2.45	DB	AAA	Aaa	
23 Apr 19	Inter-American Development Bank	500	23 Apr 24	Fixed	1.95	ANZ, CB, JPM	AAA	Aaa	
23 Apr 19	Woolworths	400	23 Apr 24	Fixed	2.85	ANZ, Citi, JPM	BBB	Baa2	
6 Jun 19	BNG Bank	300	26 Nov 25	Fixed	1.90	Nomura, RBC	AAA	Aaa	
11 Jun 19	European Investment Bank	400	15 Nov 24	Fixed	1.70	Nomura, RBC, TD	AAA	Aaa	
22 Jul 19	BNG Bank	100	26 Nov 25	Fixed	1.90	Nomura, RBC	AAA	Aaa	
24 Jul 19	KfW Bankengruppe	450	24 Jul 24	Fixed	1.50	DB, RBC, TD	AAA	Aaa	
6 Aug 19	European Investment Bank	150	3 Feb 28	Fixed	3.30	Citi, DB, Nomura	AAA	Aaa	
15 Aug 19	QIC Finance Shopping Centre Fund	200	15 Aug 25	Fixed	2.00	CB, NAB	A-		
15 Aug 19	QIC Finance Shopping Centre Fund	100	15 Aug 25	FRN	127/BBSW	CB, NAB	A-		
18 Sep 19	Asian Development Bank	150	18 Mar 30	Fixed	1.60	DB, Mizuho, RBC	AAA	Aaa	
1 Oct 19	MUFG Bank	400	1 Oct 24	FRN	125/BBSW	ANZ, MS, MUFG, NAB, WIB	A-	A1	A
1 Oct 19	MUFG Bank	100	1 Oct 24	Fixed	2.0777	ANZ, MS, MUFG, NAB, WIB	A-	A1	A
21 Nov 19	New South Wales Treasury Corporation	1,800	21 Nov 19	Fixed	1.25	ANZ, BAML, NAB	AAA	Aaa	
22 Nov 19	Macquarie University	160	22 May 30	Fixed	2.25	HSBC, NAB		Aa2	
22 Nov 19	Macquarie University	90	22 Nov 44	Fixed	3.10	HSBC, NAB		Aa2	
27 Nov 19	National Housing Finance and Investment Corporation	315	27 Nov 19	Fixed	1.52	ANZ, UBS, WIB	AAA		

SETTLEMENT DATE	ISSUER	VOLUME (A$M)	MATURITY	COUPON TYPE	COUPON(%) /MGN. (BP)	BOOKRUNNER(S)	ISSUER RATING		
							S&P	MOODY'S	FITCH
2 Dec 19	Bank Australia	125	2 Dec 22	FRN	90/BBSW	ANZ, NAB	BBB	Baa1	
2 Dec 19	NextEra Energy	500	20 Nov 26	Fixed	2.20	JPM, RBC	BBB+	Baa1	A-
3 Dec 19	World Bank	125	26 Nov 25	Fixed	2.90	Nomura	AAA	Aaa	
5 Dec 19	OCBC Sydney Branch	500	5 Dec 22	FRN	63/BBSW	OCBC, ANZ, BNPP, CB, WIB	AA-	Aa1	AA-
12 Dec 19	Uniting Financial Services	30	12 Dec 29	FRN	325/BBSW	ANZ			

NOTE: Excludes deals from Teachers Mutual Bank, which are general corporate purpose bonds. The bond programme of Teachers Mutual Bank has an ethical certification from the Responsible Investment Association of Australasia.

Cumulative Australian market GSS bond league tables

(INCLUDING SELF-LED DEALS)
1 JAN 2014 – 31 DEC 2019

BOOKRUNNER	VOLUME A$M	NO. DEALS	% TOTAL VOLUME[1]
National Australia Bank	3,629	15	17.2
ANZ	3,330	16	15.8
RBC Capital Markets	1,908	13	9.0
TD Securities	1,688	11	8.0
J.P. Morgan	1,643	10	7.8
Nomura	1,711	14	8.1
Bank of America	1,450	3	6.9
Westpac Institutional Bank	1,372	6	6.5
Commonwealth Bank of Australia	1,350	7	6.4
UBS	1,029	5	4.9
Deutsche Bank	1,027	9	4.9
HSBC	250	4	1.2
Citi	183	2	0.9
OCBC	100	1	0.5
BNPP	100	1	0.5
MUFG	100	1	0.5
Morgan Stanley	100	1	0.5
Daiwa	70	5	0.3
Mizuho	50	1	0.2
TOTAL	**21,090**		**100**

(EXCLUDING SELF-LED DEALS)
1 JAN 2014 – 31 DEC 2019

BOOKRUNNER	VOLUME A$M	NO. DEALS	% TOTAL VOLUME
National Australia Bank	2,829	13	15.4
ANZ	2,730	15	14.9
TD Securities	1,688	11	9.2
J.P. Morgan	1,643	10	9.0
Nomura	1,711	14	9.3
RBC Capital Markets	1,908	13	10.4
UBS	1,029	5	5.6
Bank of America	1,450	3	7.9
Deutsche Bank	1,027	9	5.6
Westpac Institutional Bank	872	5	4.8
Commonwealth Bank of Australia	700	6	3.8
Citi	183	2	1.0
HSBC	250	4	1.4
Daiwa	70	5	0.4
Mizuho	50	1	0.3
BNPP	100	1	0.5
Morgan Stanley	100	1	0.5
TOTAL	**18,340**		**100**

2019 Australian market GSS bond league tables

(INCLUDING SELF-LED DEALS)
1 JAN – 31 DEC 2019

BOOKRUNNER	VOLUME A$M	NO. DEALS	% TOTAL VOLUME[1]
ANZ	1,455	9	14.3
National Australia Bank	1,454	7	14.2
Nomura	842	6	8.2
Deutsche Bank	827	6	8.1
TD Securities	817	4	8.0
RBC Capital Markets	783	6	7.7
Westpac Institutional Bank	722	4	7.1
J.P. Morgan	683	4	6.7
UBS	679	3	6.7
Bank of America	600	1	5.9
Commonwealth Bank of Australia	550	4	5.4
Citi	183	2	1.8
HSBC	125	2	1.2
BNP Paribas	100	1	1.0
Morgan Stanley	100	1	1.0
MUFG Securities	100	1	1.0
OCBC Bank	100	1	1.0
Mizuho	50	1	0.5
Daiwa	40	2	0.4
TOTAL	**10,210**		**100**

(EXCLUDING SELF-LED DEALS)
1 JAN 2014 – 31 DEC 2019

BOOKRUNNER	VOLUME A$M	NO. DEALS	% TOTAL VOLUME[1]
ANZ	1,455	9	14.5
National Australia Bank	1,454	7	14.5
Nomura	842	6	8.4
Deutsche Bank	827	6	8.3
TD Securities	817	4	8.2
RBC Capital Markets	783	6	7.8
Westpac Institutional Bank	722	4	7.2
J.P. Morgan	683	4	6.8
UBS	679	3	6.8
Bank of America	600	1	6.0
Commonwealth Bank of Australia	550	4	5.5
Citi	183	2	1.8
HSBC	125	2	1.2
BNP Paribas	100	1	1.0
Morgan Stanley	100	1	1.0
Mizuho	50	1	0.5
Daiwa	40	2	0.4
TOTAL	**10,010**		**100**

CRITERIA FOR AUD GSS BOND LEAGUE TABLES: Must be use-of-proceeds bond; no minimum size; one-year minimum maturity or call date; dual-tranche issues counted as one deal if both tranches have the same maturity date; settlement date used for date calculations; issued in AUD; no requirements regarding domicile of issuer; pricing must be disclosed; deal must be syndicated; bookrunners given equal allocation (unless advised otherwise); excludes bonds that have been retrospectively labelled as green, social or sustainable bonds; excludes asset-backed securities.

SOURCE: KANGANEWS 31 DECEMBER 2019

KangaNews events diary

KangaNews runs the most comprehensive suite of events in the Australasian debt market, acclaimed by delegates for the quality of their agendas, speakers and attendees. Information on forthcoming KangaNews events is available at **www.kanganews.com/events**. Make sure to look out for the following in 2020:

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KangaNews Mutual Sector Wholesale Funding Seminar The only event focused exclusively on funding for mutual banks returns.

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KangaNews Debt Capital Markets Summit The unmissable event for the Australian debt market.

24 MARCH 2020 SYDNEY
KangaNews Sustainable Debt Summit Australia's leading conference for sustainable capital markets.

26 MARCH 2020 WELLINGTON
KangaNews-ANZ New Zealand Capital Markets Forum The scene-setter for the year ahead in New Zealand's debt market.

6 AUGUST 2020 AUCKLAND
KangaNews New Zealand Debt Capital Markets Summit The comprehensive view on the New Zealand market.

19 AUGUST 2020 SYDNEY
KangaNews-NAB Fixed Income Beyond the Institutional Sector Expanding the Australian fixed-income investor base.

14 OCTOBER 2020 SYDNEY
KangaNews-Westpac Corporate Debt Summit All the latest trends in corporate funding.

NOVEMBER 2020 AUCKLAND
KangaNews-Westpac New Zealand Sustainable Finance Summit The event for New Zealand's emerging sustainable finance market.

If you are interested in finding out more about any KangaNews event, including sponsorship opportunities, please contact Jeremy Masters: **+61 2 8256 5577** or **jmasters@kanganews.com**