THE GREEN+ BOND

HOW EU SOVEREIGN AND CORPORATE ISSUERS COULD DELIVER GREEN BONDS WITH SOCIAL CO-BENEFITS

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KEY POINTS

- We propose a new green bond that supports both a green recovery and social renewal - a "Green+" Bond.
- This new generation of Green+ Bonds would enable the EU to deliver the European Commission's new Strategy for "financing the transition to a sustainable economy."[1]
- Building on the record demand for the EU's inaugural green bond, connecting green financing with positive social co-benefits would enlist the global capital markets to support urgent public and private green projects to achieve net-zero targets and provide economic stimulus while supporting a just and inclusive transition.
- EU sovereign issuers (including the EU), public financial institutions, corporates and municipalities could all adopt this approach, building on recognised foundations for green, social and sustainability bonds.
- It would assist the Just Transition while the EU develops its social taxonomy, and would help to navigate the social taxonomy's interaction with the existing Environmental Taxonomy.
- This briefing note sets out a practical approach to deploy Green+ Bonds to contribute to the next phase of EU action on sustainable finance.

[1] Source: EU Commission

OVERVIEW

We welcome the Commission's ambitious new Strategy – including the proposed European Green Bond Standard (EUGBS) which provides a voluntary standard for all types of bonds, sovereign and corporate, EU and International, using the foundation of the Environmental Taxonomy. In particular, we note the requirement that issuers meet minimum social safeguards.

The EU has exponentially increased its bond issuance activity through an ambitious plan to fund its two COVID-19 support programmes. It will raise 30% of the €750 billion NextGenerationEU budget through green bonds.[2] This action is welcome given the urgency of the pandemic, economic and climate crises. Investors have responded well, meeting the EU's recent inaugural green bond with record demand. Corporates have also responded to the increased demand for green bonds: the green and sustainable corporate bond market has grown from €82bn in 2014 to above €700bn in 2020.[3]

In its new Strategy, the Commission recognises that the recovery from the COVID-19 pandemic has highlighted the need for a Just Transition supporting workers and their communities affected by the transitioning of economic activities across Member States. The Platform on Sustainable Finance's recent draft report for a social taxonomy underlines this. There is an urgent need to focus on these social issues and economic stimulus alongside the transition to net-zero. Thus, we propose that the EUGBS include an expansive social baseline including an emphasis on the social co-benefits of green projects supporting a Just Transition.

This Green+ Bond model would mark an important step forward in the development of the global green bond market by showing how the use of proceeds can simultaneously deliver environmental benefits, tackle inequality, build economic resilience and help the global community achieve a Just Transition. Its focus on social co-benefits would complement the GBS framework as proposed by the Commission within the context of the Commission's new Strategy for financing the transition to a sustainable economy. ***It would build on the existing minimum social safeguards in the Environmental Taxonomy to target a Just Transition and achieve sustainable development. This would focus on social and economic co-benefits in the shorter term while a broader social taxonomy is in development.***

In sum, a Green+ Bond could help support the EU's net-zero target, providing an effective tool for corporates. It would deliver four main benefits:

1. **Environmental**: tackle climate change and other environmental issues by creating funding for projects that contribute to a resilient, net-zero and nature-positive economic recovery.
2. **Social:** address the need for a Just Transition - with an emphasis on green jobs, building new skills and further education.
3. **Systemic:** catalyse further global green issuance and develop green finance and broader sustainability expertise.
4. **Global**: leverage the momentum of recent European green bond issuances and encourage sovereigns and corporates around the world to issue similar types of bonds recognising social co-benefits.

[2] Source: EU Commission
[3] Source: BMO Financial Group (January 2021); Figures converted from £ to € via XE Money Transfer Rates (March 2021)

CHANNELING FINANCE TO A RESILIENT, NET-ZERO ECONOMY

The first dimension of the Green+ Bond is to channel finance to support the Paris Agreement and the commitment of signatories to a resilient, net-zero economy. We have identified four priority categories, which respond to the EU's Just Transition Mechanism and new Strategy for financing the transition to a sustainable economy and accord with previous corporate and sovereign green bond issuance. Proceeds would be used to finance activities which make a substantial contribution to Climate Change Mitigation and Adaptation objectives under the EU Taxonomy Regulation while also fulfilling "do no significant harm" criteria and meeting minimum safeguards – for example:

PRIORITY CATEGORIES	SUBCATEGORIES	SOCIAL IMPACT
CLEAN INFRASTRUCTURE	Affordable Clean Energy: renewable generation & distribution Clean Transport: rail, electric vehicle & charging infrastructure Industrial Decarbonisation: carbon emissions management, capture & storage in sectors such as cement and steel, hydrogen networks	Generation of 'decent work' opportunities Tackling regional inequalities Access to basic infrastructure (energy) Access to basic infrastructure (transport)
ENERGY EFFICIENCY & GREEN BUILDINGS	Spending on the energy efficiency of new housing (including affordable/social housing), and renovations and retrofits including improved insulation, heating and domestic energy storage systems	Generation of 'decent work' opportunities Tackling regional inequalities Access to housing built to green standards
CLIMATE ADAPTATION & NATURAL CAPITAL	Investment in biodiversity regeneration and a zero-pollution ambition, including flood defence mechanisms, restoration of carbon-rich habitats, climate-friendly agriculture and clean water	Protecting local, vulnerable communities and respecting their rights Generation of 'decent work' opportunities Tackling regional inequalities
GREEN JOBS	Investment in reskilling and education in connection with the activities above and others with a Climate Mitigation and/or Adaption objective - with an emphasis on addressing structural shifts due to decarbonisation (ensuring a Just Transition)	Generation of 'decent work' opportunities Tackling regional inequalities
GREEN FINANCE DEVELOPMENT	Helping to fund regional and national investment banks with a sustainability mandate, seeking out net-zero aligned projects for which risk levels need to be reduced	Capture-all category

GENERATING JOBS AND SOCIAL RENEWAL

The novel feature of the proposed Green+ Bond is that financed projects would focus attention on **'social co-benefits'** in addition to environmental outcomes, thereby contributing to a **Just Transition.**

Careful allocation of the Green+ Bond proceeds to the right projects with robust reporting will demonstrate how environmentally sound investments can create high-quality jobs and contribute to supporting human rights and reducing inequalities. This would help to ensure that the cost of the transition is not borne by those in society least able to afford it.

Drawing on the ICMA Social Bond Principles (SBP), each eligible project would have at least one well defined and measurable social co-benefit, with a relevant social metric for each project category. These could include outcomes such as affordable housing and infrastructure, generation of 'decent work' opportunities, access to essential services, skills development and education as well as other aspects of socioeconomic advancement. Social co-benefits could also be generated by allocating public and private finance to Taxonomy- compliant projects in areas of relative deprivation.

Currently, there are three recognised types of "labelled" bonds designed to address sustainability challenges. The most well-established of these are green bonds that allocate proceeds to environmental projects, whereas more recent innovations include social bonds and sustainability bonds; the former focused on social outcomes and the latter allocating proceeds to a combination of both social and environmental programmes.

Sustainable debt issuance supply has grown rapidly in response to the global pandemic. Bonds and loans with environmental and social purposes reached €633bn in 2020, a year-on-year increase of 29%. This was led by the growth of social bonds, which rose sevenfold to €128bn in 2020.[4]

We welcome the increased investor appetite for social bonds alongside green – but our Green+ approach is required to truly capitalise on this and reflect the reality of the Just Transition. All green projects have social implications; therefore, all green bond issuance should include social co-benefits.

The Green+ Bond proposal recognises these market developments and would provide sovereign and corporate access to the broad universe of green investors, to ensure the greatest demand and tightest pricing, whilst also facilitating a Just Transition and generating social benefits in line with EU objectives.

The addition of social co-benefits with well-defined social metrics for each project was widely welcomed by the investors we have consulted, with the focus on jobs and skills particularly well received.

The inclusion of practical social co-benefits within green spending would also assist the EU's development of a social taxonomy, particularly regarding its interaction with the existing Environmental Taxonomy.

[4] Source: BloombergNEF (January 2021); Figures converted from $ to € via XE Money Transfer Rates (October 2021)

PROVEN COST-EFFECTIVENESS AND DIVERSIFICATION OF INVESTORS

To date, 18 countries have issued green bonds.[5] The EU also recently issued its inaugural green bond, attracting more than €135bn of orders on a €12bn sale. These sovereign green bonds have secured a cost of capital that is generally comparable to conventional non-green issuance. They have also catalysed growth of the green bond market more generally.

Corporate green bonds have shown a similar rise in demand: approximately €163bn of green or sustainable corporate bonds were issued in 2020 globally, 12.5% more than 2019.[6]

The Green+ Bond aligns with the Commission's ongoing work stemming from the Sustainable Finance Action Plan, and new Strategy for financing the transition to a sustainable economy. At the EU level, the objective remains supporting the economic green transition and expanding focus to the real economy.

A Green+ Bond would heighten market interest in green bonds, attracting the growing pool of green bond investors – and those who wish to support economic and social renewal and encourage international investors to fund related projects.

THE BENEFITS IN BRIEF

To date, 18 countries have issued green bonds, consistently achieving an equal or lower cost of capital for the public finances. The corporate green bond market has also grown significantly in recent years, as issuers respond to growing demand in the EU and globally.

A Green+ Bond would:

- Support a Green Recovery, Capital Markets Union Action Plan and the Commission's new Strategy for financing the transition to a sustainable economy by developing the green capital markets with an emphasis on a Just Transition.
- Underpin a sustainable economic recovery by directing proceeds to the growing net-zero economy while at the same time creating high-quality jobs and other social benefits.
- Provide investment to enhance productivity by upgrading infrastructure, supporting innovation and building skills.
- Respond to rising investor demand by providing a liquid instrument that can feature in every relevant portfolio.
- Establish a global framework for Green+ Bond issuances that builds economic confidence on the road out of the COVID-19 crisis and to a Just Transition.
- Support the EU's development of a social taxonomy, particularly regarding its interaction with the existing Environmental Taxonomy.

[5] Seven countries have also issued other use of proceeds labelled bonds.
[6] Source: BMO Financial Group (January 2021); Figures converted from £ to € via XE Money Transfer Rates (March 2021)