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“MAKE OUR PLANET GREAT AGAIN” – GREEN, SOCIAL AND SUSTAINABILITY BONDS

This short alert highlights some of the key themes discussed at the Green Bond Principles 3rd AGM and Annual Conference in Paris on 14 June 2017, the changes made to the Green Bond Principles and the launch of the Social Bond Principles and Sustainability Bond Guidelines.

The conference was very well attended and participants were enthusiastic and confident about the growth and developments in the market. The unofficial motto, as seen on badges worn by participants, was “Make our Planet Great Again”. There was particular focus on the French Government’s inaugural €7bn green bond in January and the impact of the Chinese green bond market, reportedly worth US\$23bn in 2016, according to figures from the Climate Bonds Initiative. Honourable mention also went to the various initiatives outside of the GBP, such as the establishment of the European Commission’s High-Level Expert Group on sustainable finance, plus the work done by the Climate Bonds Initiative and the Task Force on Climate Related Financial Disclosures, as well as the continuing support of the multilateral development banks.

The Green Bond Principles (GBP)

The GBP themselves were little changed from 2016 (see GBP 2017 changes text box) which no doubt reflects the confidence that the key GBP stakeholders, issuers, investors and underwriters, have in the industry standards which have been developed and the current performance of the market. More interesting, perhaps, are the views and opinions expressed at the conference as to developments over the last year. There seems to be a general

shift away from the previously perennial question as to what is “green” and a broader focus instead on how the GBP, with its cornerstone principle of use of proceeds, can facilitate and support all issuers, including “brown” issuers, move towards a more sustainable future. Transparency remains key and issuers in controversial sectors will especially have to provide a strong and compelling narrative to investors of their overall environmental strategy and sustainability goals.

There was also enthusiastic recognition of the emergence of new types of issuers, particularly sovereigns, and new products, for example green ABS and hybrids, and the growth of other green financing options, such as green loans. Discussions reflected that, whilst the GBP themselves remain relatively unchanged, the GBP working groups and other market participants continue to focus efforts on understanding taxonomies across different initiatives and developing reporting and impact assessment models and standards.

New Questions & Answers

The resources available to green bond market participants continue to grow. Building on the launch of the GBP Resource Centre last year, in which issuers are encouraged to publish their short form market information document and external reviews, the GBP have launched a detailed Q&A, including

GBP 2017 changes

Use of Proceeds: it remains the basic principle that the proceeds of a green bond must be used to support green projects which provide clear environmental benefits. The list of green project categories has been updated to include green buildings which meet regional, national or international standards and other minor changes to existing project categories.

Process for project evaluation and selection: there is a new emphasis on communication to investors of the issuer’s environmental objectives and the green bond eligibility criteria with explicit encouragement to position this information within the issuer’s overarching objectives and policy relating to environmental sustainability.

Management of proceeds: a change to allow an amount “equal to the net proceeds” of a green bond to be tracked to a sub account has been made.

Reporting: the list of voluntary impact reporting guidelines has been expanded to include water and wastewater.

questions such as ‘Is there a definition of a green bond?’, ‘Can a project bond be a green bond?’ and ‘Can green bonds default by not following the GBP recommendations anymore?’.

As with the Resource Centre, the Q&A are available on the ICMA website under its Green, Social and Sustainability Bond page and the intention is to update these regularly.

The Social Bond Principles (SBP)

The new Social Bond Principles build on and replace the Guidance for Issuers of Social Bonds published by the GBP alongside the GBP 2016.

By way of example of Social Bonds in the market, IFC has a Social Bond Programme, which aligns with the GBP's 2016 Guidance for Issuers of Social Bonds, and includes issuance of "Banking on Women Bonds" (which support women-owned SMEs in emerging markets) and "Inclusive Business Bonds" (which support private enterprises that incorporate low-income people into their business models and supply chains).

The SBP replicate the framework and technology of the GBP but with application to distinct social projects. As with the GBP, the SBP are voluntary with a focus on disclosure and transparency to facilitate increased issuance by the market. The two sets of principles are designed to run independently side by side but with a joint governance structure comprised of (1) the member and observers, (2) the Executive Committee, (3) the Steering Committee and (4) the Secretariat.

The four core principles of the SBP are:

Use of Proceeds: the proceeds must be used for Social Projects. Social Projects are defined as projects that "directly aim to help address or mitigate a specific social issue and/or seek to achieve positive social outcomes especially, but not exclusively, for target populations". Non-exhaustive examples of social projects include provision or promotion of affordable basic infrastructure (e.g. clean drinking water and transport), affordable housing and food security (see Social Project Categories text box). Examples of target populations include those living

Social Project Categories (non-exhaustive list)

- Affordable basic infrastructure (e.g. clean drinking water, sewers, sanitation, transport)
- Access to essential services (e.g. health, education and vocation training, healthcare, financial and financial services)
- Affordable housing
- Employment generation, including through potential effect of SME financing and microfinance
- Food security
- Socioeconomic advancement and empowerment

below the poverty line and those with disabilities (see Target Population examples text box).

Process for project evaluation and selection:

the issuer must be clear about the social objectives of the bond, the process by which eligible projects are identified and the eligibility criteria. The issuer is encouraged to base this disclosure within its broader social sustainability objectives and strategy.

Management of proceeds: the issuer should have formal internal processes to allocate and track the proceeds of the social bond.

Reporting: the issuer should keep and make available up to date records on the use of proceeds. The SBP recommend use of qualitative and quantitative performance measures and, where possible, the recording and reporting on achieved impacts.

As with the GBP, an external review is recommended.

The SBP lists the four current types of bonds as: standard social use of proceeds bond; social revenue bond; social project bond; and a social securitised bond.

Sustainability bonds

The GBP and SBP recognise that certain projects to be financed by the use of proceeds will have both green and social benefits. Classification as a green or social bond should be based on the primary objective of the underlying project. However, where the proceeds will be applied to both green and social projects, the bond can be classed as a sustainability bond, if it complies with the four core components of both the GBP and the SBP.

Confirmation of this approach is set out in the Sustainability Bond Guidelines published alongside the GBP 2017 and SBP. We anticipate that there may be some initial confusion in the market given the proliferation of bonds with monikers such as "Social impact", "ESG", "Climate" and "Sustainable" but hope that the new SBP and Sustainability Bond Guidelines can play an important role in providing clarity.

Examples of target populations (non-exhaustive list)

- Living below the poverty line
- Excluded and/or marginalised populations and/or communities
- Vulnerable groups, including as a result of natural disasters
- People with disabilities
- Migrants and/or displaced persons
- Undereducated
- Underserved
- Unemployed

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