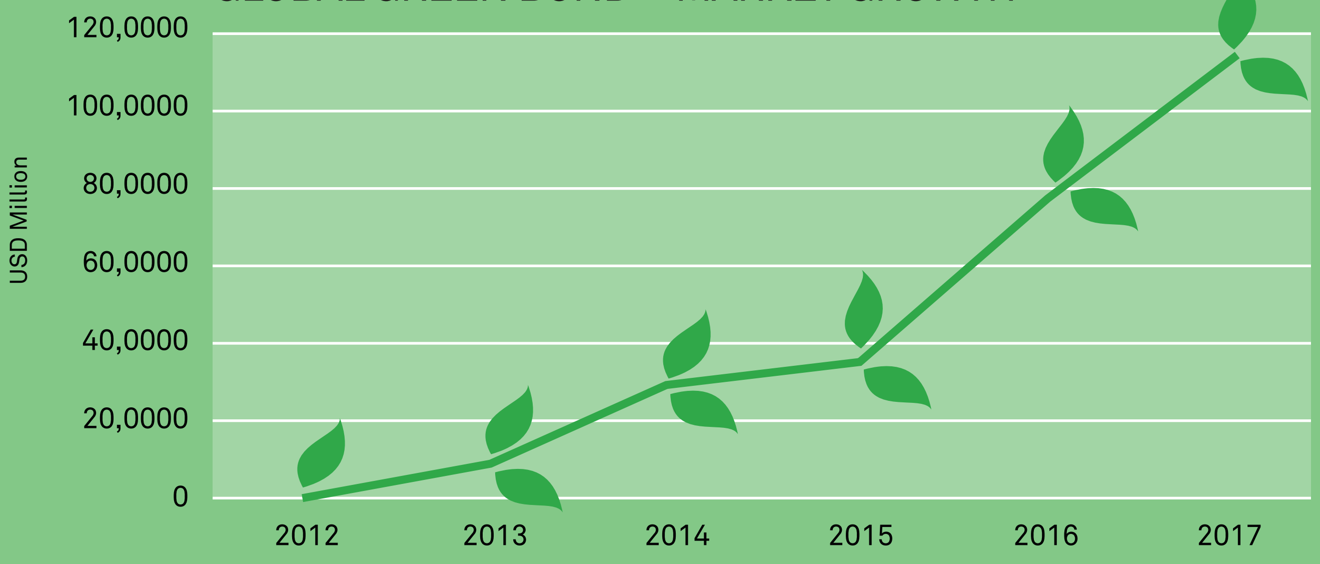
Green thinking

Green bond issuance is rising steadily...

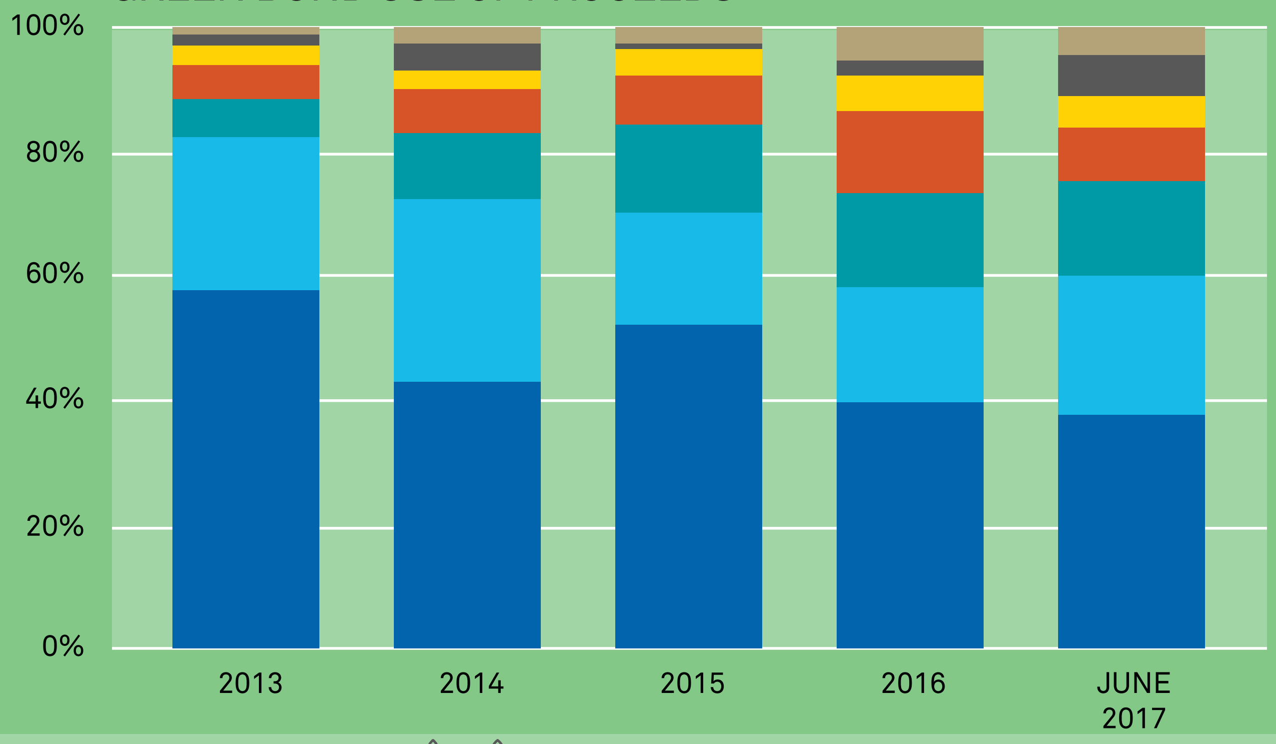
GLOBAL GREEN BOND – MARKET GROWTH

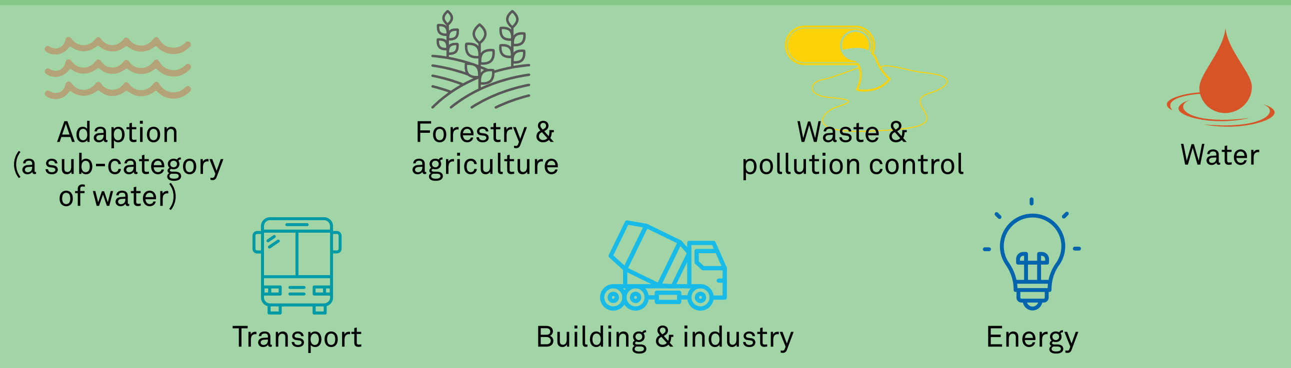


Source: Bloomberg League Tables as at 8 March 2018.

The market helps support funding a wide variety of development areas

GREEN BOND USE OF PROCEEDS

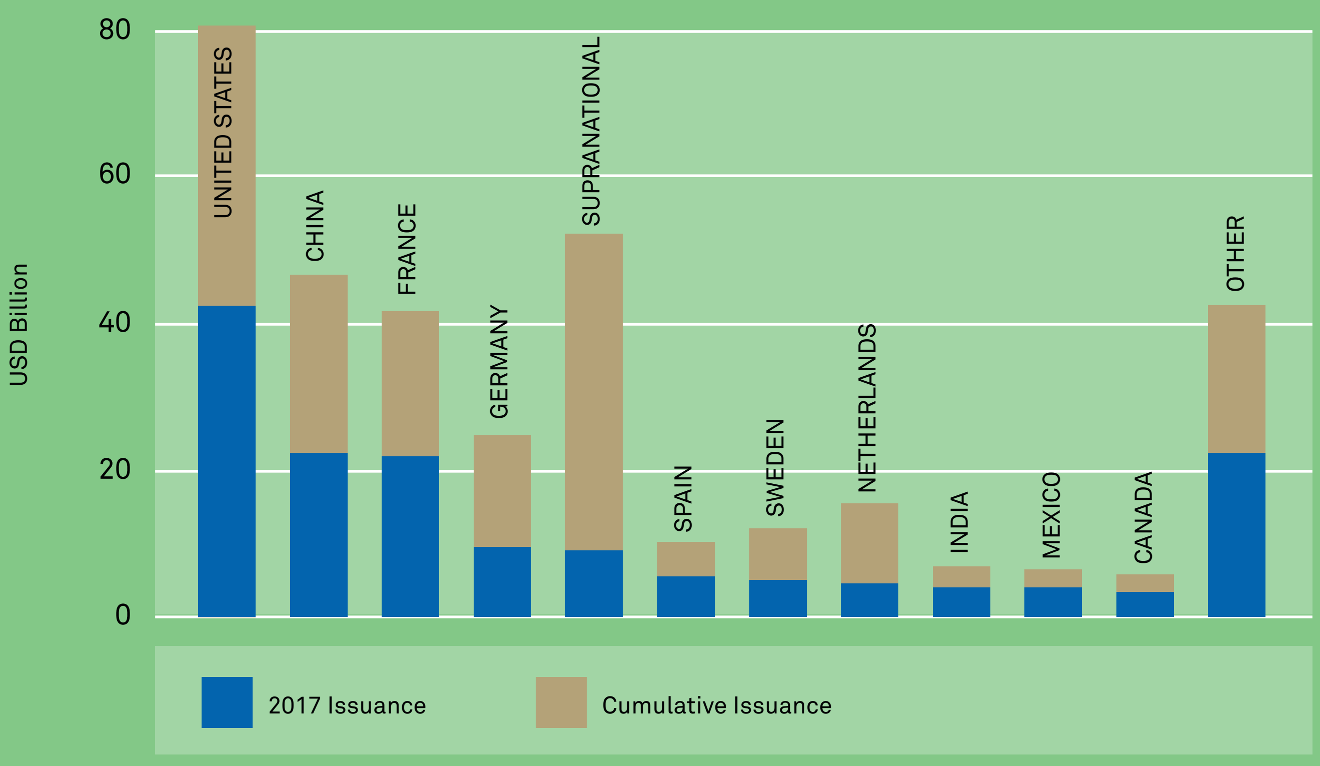




Source: Climate Bonds Initiative.

But a limited number of markets still dominates issuance with scope for further diversification and growth.

THE US, CHINA AND FRANCE DOMINATED 2017 ISSUANCE



Source: Climate Bonds Initiative as at end December 2017.

MARKETEYE
INVESTMENT IDEAS ILLUSTRATED AND SHARED

BNY MELLON

Green bonds* offer investors looking for exposure to sustainable investments a chance to invest in the 'E' (environmental element) of their environmental, social and governance (ESG) remit. They allow investors to help aid the transition to a low-carbon world by lending money that will be used for specific green projects.

Historically, exposure to these types of projects was through higher-risk and less-liquid project-finance debt. Standard 'use-of-proceeds' green bonds benefit from being backed by the underlying credit rating of the issuer, thereby lowering the specific project risk and thus overall credit risk. The cash flows funding the coupons and principal can originate from non-green operations, and the bond can still be considered 'green'.

Evidence suggests that green bonds price at a similar spread to non-green bonds, thereby encouraging investors who do not have specific green mandates to consider investing in them, but the market remains relatively niche.

The real boost that the asset class needs will come when companies from a wider range of industries and geographies are encouraged to enter the market, which will increase liquidity. Countries issuing green bonds may help lead by example.

The fact that green bonds are becoming higher profile leads us to expect that the market structure will continue to improve over time. However, if the market is to continue to grow strongly, it will need greater diversification across credit rating, sector and geography in order to improve liquidity, and a globally agreed means of assessing and evaluating individual bonds.

Scott Freedman – analyst and portfolio manager fixed income team at Newton, a BNY Mellon company

* Bonds are subject to interest rate, credit, liquidity, call and market risks, to varying degrees. Generally, all other factors being equal, bond prices are inversely related to interest-rate changes and rate increases can cause price declines. Municipal income may be subject to state and local taxes. Some income may be subject to the federal alternative minimum tax for certain investors. Capital gains, if any, are taxable. High yield bonds involve increased credit and liquidity risk than higher rated bonds and are considered speculative in terms of the issuer's ability to pay interest and repay principal on a timely basis.

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