Green Bonds

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With growing concerns about global warming, a fairly new type of bond emerged, known as the Green Bond. It is a fixed-income instrument that has been set aside to raise money for green projects.

Green bonds were developed by the World Bank and the European Investment Bank more than 10 years ago and are used to finance sustainable projects related to energy efficiency, pollution prevention, sustainable agriculture, forestry and fishery, the protection of ecosystems, clean transportation, clean water and sustainable water management.

The first emerging-market green bond was issued in South Africa in 2012. Poland opened the sovereign market in 2016, followed by the likes of France, Belgium and Ireland.

Why green bonds?

Investors are increasingly demanding socially responsible investment opportunities and have expressed a strong appetite for green bonds by repeatedly oversubscribing issuances. While retail investors demand sustainable investments from their brokers and fund managers, institutional investors are using green bonds to address ESG (Environment, Social, and Governance) mandates, something that, before Green Bonds, had been a struggle to address with fixed income tools. As a result, green bond issuances have attracted new investors and new types of investors, providing a potential market for future issuances.

Green bonds are an excellent way to secure large amounts of capital to support environmental investments that may not otherwise be available, or that may be uneconomic using more expensive capital. Green bonds are well suited for large-scale sustainability projects such as wind and solar development, which often require capital investment ahead of revenues, and which generate modest revenue over a longer investment horizon.

Green bonds provide investors with a way to earn tax-exempt income with the benefit of knowing that the proceeds of their investment are being used in a responsible, positive manner. The issuers of green bonds also benefit, since the green angle can help attract a new subset of younger investors—whom the issuers can profit from over an extended period.

Investing in Green Bonds provides the investor with a chance to brand themselves, in case of a company, as forward thinking, innovative, and sustainable. All of these being a great tool for CSR.

Who buys green bonds?

Just as any other bond market, institutionalized investors, including pension funds, insurance companies and asset managers invest in green bonds. The overall green market is also getting a boost from investors seeking “responsible” or “sustainable” places to put their money.

Challenges

While green bonds were created to curb climate issues, ensuring whether the impact that the green bond has on the environment is transparent, verifiable, measurable and compliant with international standards is still a concern.

Green bonds generally yield lower returns than traditional bonds.