# Global sustainable finance market: changing for the better

The global sustainable finance market continues to see decent levels of issuance and new areas of growth in 2024. Green bonds are experiencing strong momentum while KPI-linked debt has embraced innovation and quality improvement. Europe still dominates the market. Meanwhile, elections around the world add to the risk of policy disruption

We could see decent global sustainable finance issuance in 2024 after the down years of 2022 and 2023

Global sustainable finance issuance volumes have retreated from the peak in 2021, which at the time was driven by a flurry of company sustainability targets, a Covid 19-induced surge in social debt, and an Environmental, Social and Governance (ESG) market where enthusiasm trumped scrutiny. Issuance then declined in 2022 and 2023. Policy disruption has curbed the confidence of some issuers, and increased ESG controversy and scrutiny over green credibility have led to stricter issuance standards and a preference for quality over quantity.

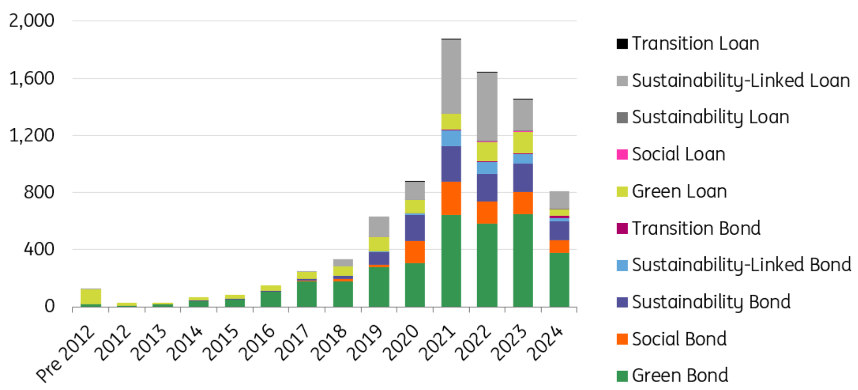
Looking forward, we argue that we could see a decent issuance level in 2024 as companies need to demonstrate on-schedule progress towards sustainability targets as well as an increase in green capex, and sustainable finance remains a key tool to help achieve that. Meanwhile, the emergence of innovative products can help to keep the sustainable finance market attractive.

## Global issuance in 2024 could match 2023 levels

In the first half of 2024, issuance of sustainable debt around the world reached $800bn, almost at the same level as that in the first half of 2023. This shows that the global sustainable finance market has so far this year been able to maintain the momentum seen in 2023. Issuance in the second half of 2023 was at $640bn, the lowest half since 2021. This year, any improvement from that level would result in an increase in the annual volume in 2024, which is now probable.

## Global sustainable finance issuance

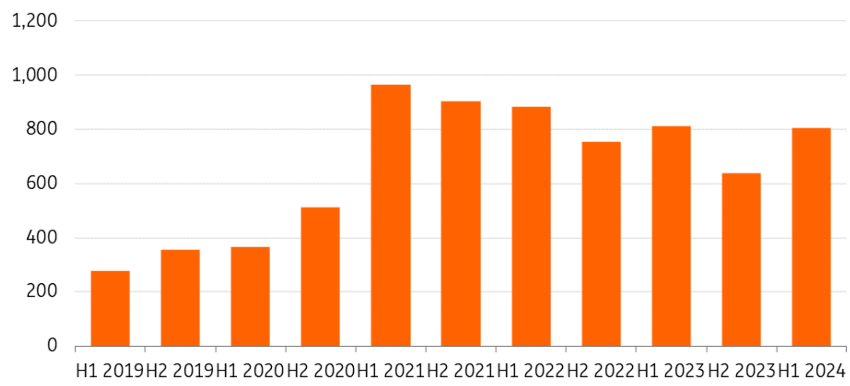
$bn




Data is until 30 June 2024. Source: Bloomberg New Energy Finance, ING Research

## Global sustainable finance issuance

$bn (half year on half year)




Data is until 30 June 2024. Source: Bloomberg New Energy Finance, ING Research

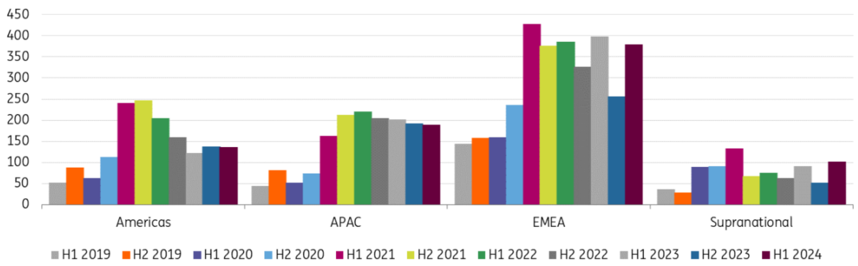
## EMEA still dominates sustainable debt issuance

EMEA, led by Europe, remains the largest region in terms of sustainable finance issuance with a strong rebound in volumes in the first half of 2024. The EU's more comprehensive and advanced ESG regulation ecosystem helps. It is true that recently, the perceived cost of energy transition, and rising populism have led to a stronger right-wing presence in the European Parliament.

However, we don't expect the EU's green agenda to change fundamentally.

## Sustainable finance issuance by region

$bn




Data is until 30 June 2024. Source: Bloomberg New Energy Finance, ING Research

In the Americas, issuance has been somewhat stable during the past 18 months. The market has shown some degree of resiliency despite divided ESG viewpoints and concerns about disruptions from the US elections. If the Republican party takes over the White House, we may see more reluctance from companies to label their debt as sustainable or ESG, although they are likely to carry on with sustainability efforts.

A significant positive spin in the Americas is the Inflation Reduction Act (IRA). The law has spurred over $200bn of investment in clean energy manufacturing, making it unlikely to be repealed entirely despite possible downsizing. It would continue to be a key piece of legislation driving sustainable activities in the US.

APAC is growing into a robust sustainable finance market, with rising clean energy investment providing a favourable environment. Moreover, the region is catching up on sustainable finance policy. Jurisdictions including China, Japan, South Korea, Philippines, Singapore, Malaysia, Bangladesh, and Australia intend to incorporate the International Sustainability Standards Board's (ISSB's) sustainability reporting standards. Most regimes have fast-approaching initial implementation dates in 2025 or 2026.

Nonetheless, a significant challenge that APAC faces is the implementation of green debt principles in sectors with high emissions, without compromising the integrity of these standards. China, for instance, updated its GBP in 2022 to require 100% of the use of proceeds on green projects to align with the International Capital Market Association (ICMA). But state-owned companies are still exempt and only need to allocate 50% of the use of proceeds to green projects. In Japan, where the country's Green Bond Guidelines are aligned with the ICMA, transition bonds are thriving as a new way to finance decarbonisation in sectors that have a significant environmental impact.

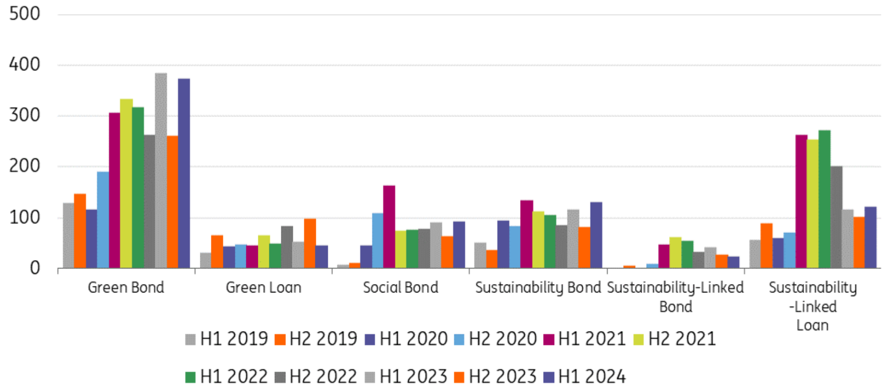
## Green bonds hold strong while KPI-linked debt embraces quality improvement

Breaking down issuance by product, we can see that in the first half of 2024, green bonds contributed the most to the global total, and the issuance volume was the second-highest for any half-year period. Green bonds experienced a jump in issuance volume in the first half of 2024 compared to the second half of 2023, while the number of issuances in the two halves is almost the same. This means that the high volume seen in the first half of 2024 is largely because of several sizable (ranging from $6.6bn to $9.7bn) issuances, including those from the government of Italy, the government of France, and the EU. It is true that government agencies, sovereigns, municipal, and supranationals accounted for the largest share of green bond issuance in the first six months of 2024, at 42%, but the share of corporates increased from 25% in 2023 to 32% in the first half of 2024, while the share of issuance from financials decreased from 30% to 22% over the same period.

With relatively more advanced green bond frameworks laying out detailed guidelines for eligible project selection, use of proceeds allocation, and impact reporting, green bonds will continue to be the growth engine for the global sustainable finance market. Nevertheless, there is both anecdotal and empirical evidence indicating a resurgence of interest in social and sustainability bonds, as investors broaden their focus to include concerns beyond mere emissions.

## Global sustainable finance product issuance trends

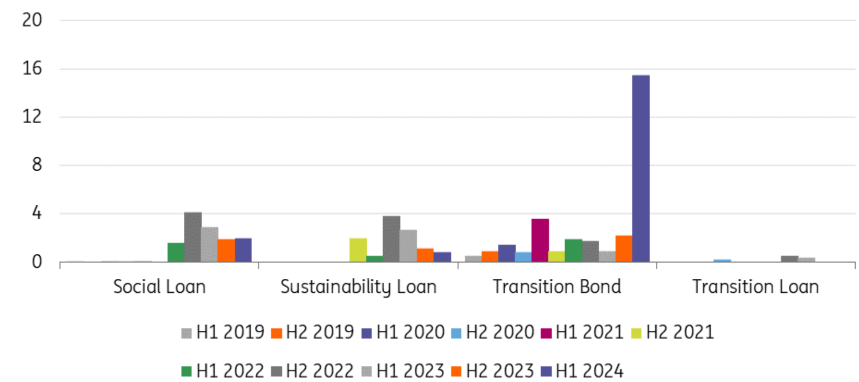
$bn




Data is until 30 June 2024. Source: Bloomberg New Energy Finance, ING Research

## Global sustainable finance product issuance trends (cont'd)

$bn




Data is until 30 June 2024. Source: Bloomberg New Energy Finance, ING Research

Another visible trend is the increasing popularity of transition bonds, whose issuance was up almost eightfold in the first half of 2024 compared to the second half of 2023. Transition bonds allow companies to finance decarbonisation activities that are not ‘traditionally green’ but can substantially reduce emissions in hard-to-abate sectors. However, it is worth noting that Japan dominates the market for transition bonds, home to $13.9bn of the $15.5bn issued volume in the first half of 2024, largely enabled by the country’s Climate Transition Bond Framework.

Outside of Japan, it appears to be challenging to issue transition bonds due to a lack of clear definitions. Nevertheless, the surge in transition bonds could indicate a higher level of openness for the market to consider transition activities and embrace product innovation. What could be helpful to this trend is the ICMA's newly published Green Enabling Projects Guidance, which defines activities that are crucial to developing a green project but do not themselves have a direct positive impact on the environment. These include the production of materials used for clean energy equipment, among others.

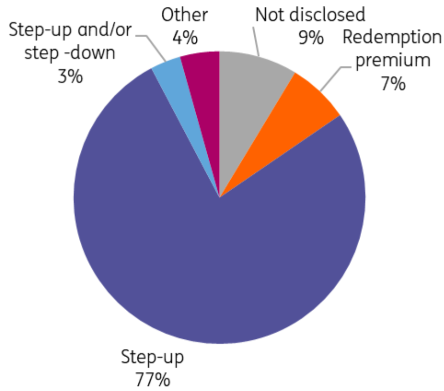
Meanwhile, the sustainability-linked bonds (SLBs) and sustainability-linked loans (SLLs) market is going through constructive changes to improve quality. Sustainability-linked debt allows companies that may not be able to easily identify eligible projects to tap into sustainable finance. Taking a KPI-based approach also allows issuers to tackle sustainability from a broader company level.

Admittedly, SLBs and SLLs have lost some popularity because of the continuing scepticism over how they can effectively demonstrate credibility. Of the 50 SLBs sampled in a recent report by the Climate Bonds Initiative (CBI), 48 report on their KPI progress, but issuers tend to fall short of detailing data reporting statements, explaining changes in performance, and keeping data consistent. And 34% of the total issued amount by the sampled issuers is linked to sustainability KPIs that are currently off track. Moreover, about half of the issued SLB amount in CBI’s larger dataset only has one linked KPI, and many of these KPIs are not sector-material.

Finally, the structure of SLBs is in need of some innovation. Coupon step-ups – meaning issuers pay penalties in interest if their sustainability KPIs are missed – are the most common structure of SLBs, representing 77% of the SLB amount issued. Such a penalty-dominated scheme, as opposed to a more incentive-based scheme where issuers are awarded for achieving their KPIs, may have discouraged SLB issuance. For the SLBs that have already been issued, an average coupon step of around 25 basis points indicates that issuers lack both strong incentives and penalty mechanisms to achieve their KPIs.

## SLB financial mechanisms

Total sample = $279.3bn



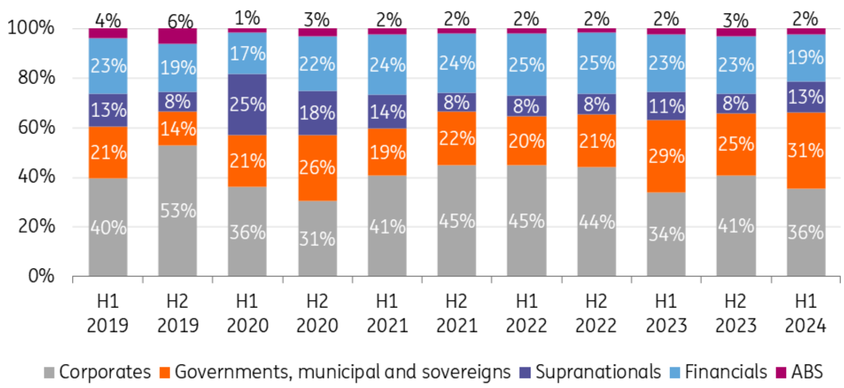

Source: Climate Bond Initiative, ING Research

These challenges show that the SLB market needs more detailed guidance – and that is where the market is heading. In June this year, the ICMA announced the Sustainability-Linked Loans financing Bond Guidelines (SLLBG) defining an instrument type to allow issuers to finance or refinance a portfolio of their SLLs. The organisation also updated its Sustainability-Linked Bond Principles with further detail on disclosure and KPI selection. In July, Crédit Agricole CIB issued its first SLL financing bond using the ICMA's SLLBG. The advancement in and innovation on sustainability-linked debt guidelines points to a positive direction of travel that could encourage more principles-aligned issuance in the future.

## The public sector continues to be the driver of growth

Government agencies, municipal, sovereigns, and supranational entities have been the growth engine for global sustainable finance issuance. Their share in the total market grew from 29% in the second half of 2022 to 44% in the first half of 2024. This can be attributed to rising awareness and action from governments to manage sustainability risks and enhance resiliency against climate change.

## Contribution of issuance to the global sustainable finance market by entity and type




Data is until 30 June 2024. Source: Bloomberg New Energy Finance, ING Research

Corporates, on the other hand, have registered declines in their contribution to global sustainable finance issuance. While this is due to reduced interest in large revolving loan facilities that are SLL structured, there is growing interest in green issuance which is likely to grow in volume with increasing capex. In absolute terms, most of the sectors, including industrials, utilities, consumer discretionary, materials, communications, and technology, still recorded half-on-half issuance growth in the first half of 2024.

Corporate ESG bonds have also been more affected by higher interest rates than vanilla bonds, government policy uncertainty, and an uneasy environment for ESG. From 2022 to 2024, the share of corporate ESG bonds in total bonds fell from 9.8% to 7.5%, while the share of corporate green bonds dropped from 6.4% to 5.3% and the share of SLBs decreased from 1.7% to 0.7% over the same period.

But with the new green enabling and SLL financing bond guidelines from the ICMA, there is reason to believe that companies across a wider array of sectors will be better equipped and more empowered to engage in sustainable finance issuance, spanning various product types

## Is there still a greenium?

One of the peculiarities of ESG (or, in many cases, “green”) issuance is the capability to trade at a premium versus regular (aka “vanilla") bonds. There is no theoretical reason why this should be the case. Green bonds are just as likely to be repaid as vanilla bonds, or in other words, there is no greater or lesser default risk attached to them (from the same issuer and without subordination). So, if green bonds command a premium, it must reflect a prevalence of demand over supply. The so-called “greenium” reflects this through the lower yield attached to green relative to vanilla bond issuance.

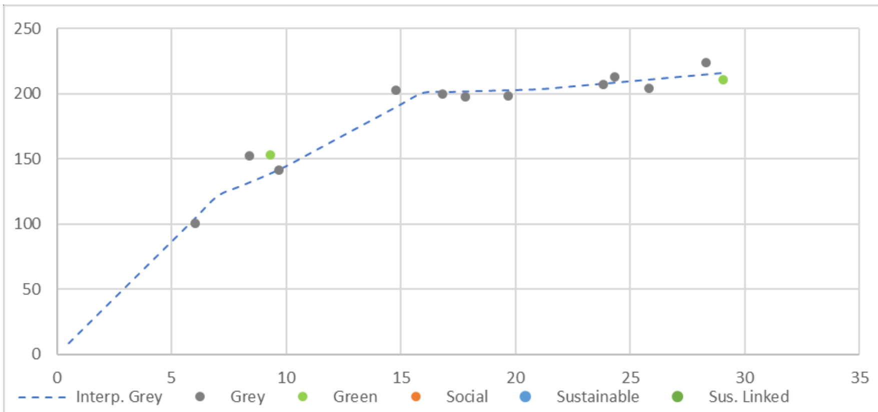
If there is a greenium, issuance in ESG bonds is cheaper for the issuer, and the buyer accepts a lower running yield. Why? It's not just because embracing ESG is seen to be the right thing to do, it is also seen as a sensible long-term investment practice. The ultra buy-and-hold strategy must embrace this, as holding on for the long term requires sustainability. At the extreme, sustainability reduces existential risk (the ultimate default). In the end though, it is all about supply and demand. As noted above, supply has waned to an extent in recent years. But so too has demand, as the space has been complicated by both regulation and a lack thereof.

Generically we’ve found that greeniums, where they exist, tend to be smaller than they were. The green novelty in more mature markets, which have been issuing in this space over several years, has waned. That in many ways comes back to the simple supply-demand effect. That said, we continue to find that syndicated books for ESG issuance tend to be a multiple of a typical deal, and tend to include a significantly wider number of interested types of investors. This does not always generate a greenium, but can push in that direction, especially where issuance circumstances are auspicious. We continue to find good investor demand for ESG issuance from emerging market issuers, which creates a tendency for a greenium to become an end-game feature.

Here, we undertake some examples for comparison across a wide set of issuance and circumstances. We take a spectrum of names across sovereign, supranational, and agency bonds (SSAs) and corporates, in euros and dollars, and from a secondary perspective and a primary perspective. The recent Dow Chemical issuance is a prime example, where a greenium was clearly evident. On the secondary market, most bonds eventually settle back in line with the curve. But there is still an echo of primary market conditions as otherwise, investors would be minded to buy on the secondary rather than the primary market (notwithstanding the size advantages to buying on primary).

Below is how the recent long-end Dow green bond has settled back onto the secondary curve when expressed in Z-spread space, with that particular issue commanding a 6bp greenium.

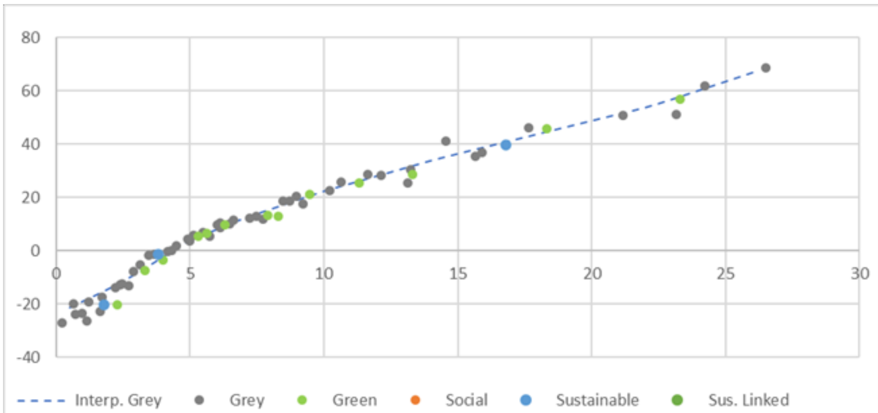
## Dow Chemical – Z spreads to dollar curve




Source: ING estimates, Macrobond

EIB in euros is below. We detect only a mild greenium in places, and on average green bonds trade with a 1.3bp greenium.

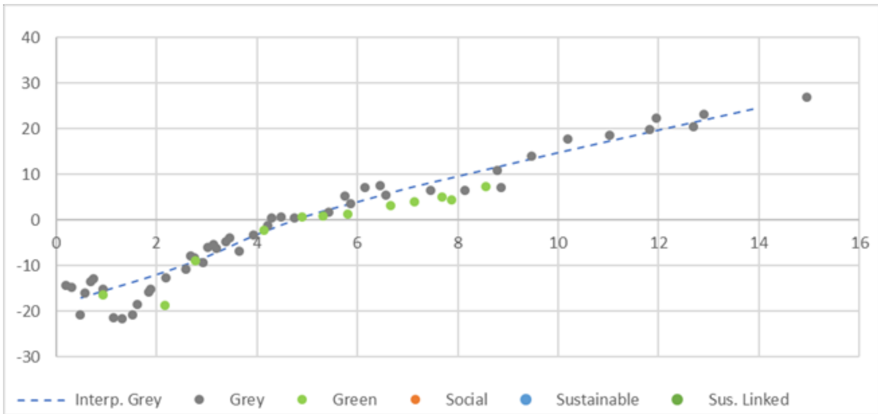
## European Investment Bank – Z spreads to euro curve




Source: ING estimates, Macrobond

For KFW in euros, in average across the entire curve, we calculate a 2.4bp greenium. But there are many specific bonds trading without a greenium.

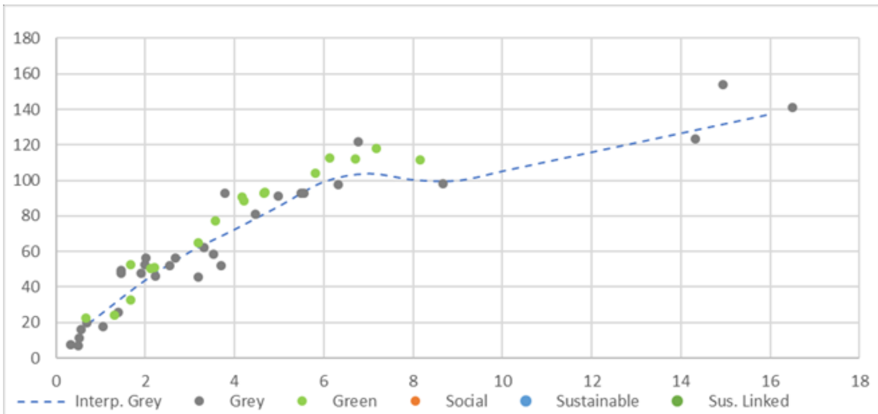
## KFW – Z spreads to euro curve




Source: ING estimates, Macrobond

Switching to corporates. Here's Volkswagen, where there is no material greenium in evidence. And note the large number of green bonds, which adds to the supply.

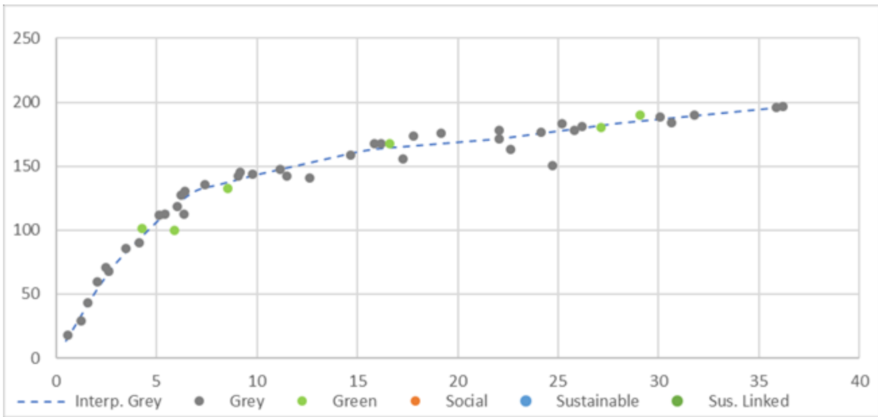
## Volkswagen – Z spreads to euro curve




Source: ING estimates, Macrobond

Contrast that with Verizon in dollars, where there is in fact some evidence of a generic greenium, which we calculate at 1.8bp on average.

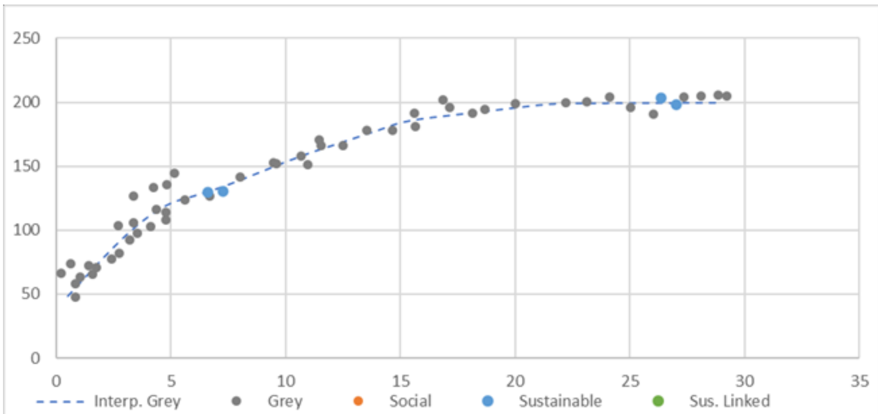
## Verizon – Z spreads to dollar curve




Source: ING estimates, Macrobond

And here's Edison International, which has issued a series of sustainable bonds. These show a very mild greenium, but it is too small (-0.2bp) to be statistically close enough to be marked effectively at zero.

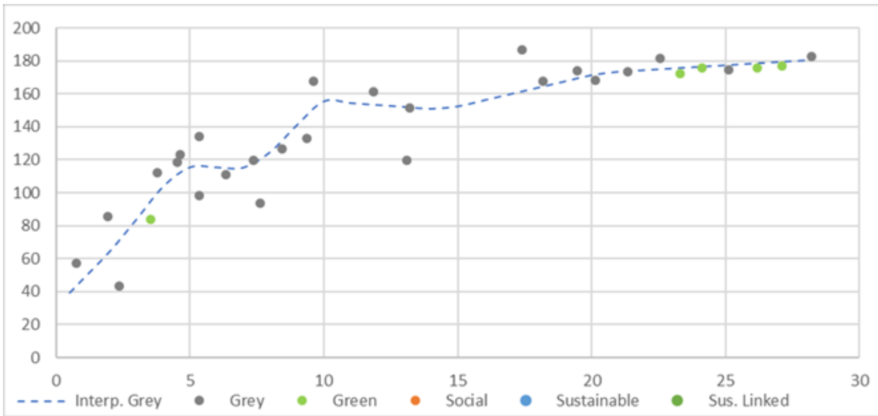
## Edison International – Z spreads to dollar curve




Source: ING estimates, Macrobond

And here's DTE in dollars, which commands an average greenium of some 4bp. But as you can glean, it depends on how the liquid curve is constructed.

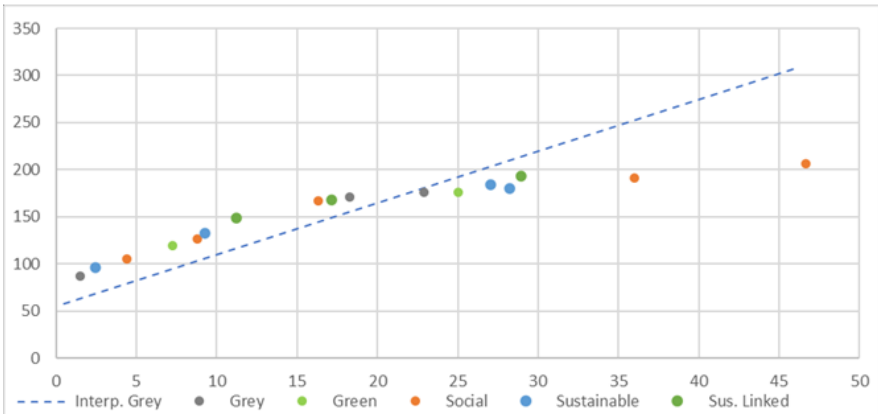
## DTE – Z spreads to dollar curve




Source: ING estimates, Macrobond

And here's one more interesting one – the government of Chile, which has been quite active in the ESG issuance space over recent years. Here, there is a greenium in social bonds, but not in green and sustainable-linked bonds.

## Government of Chile – Z spreads to dollar curve




Source: ING estimates, Macrobond

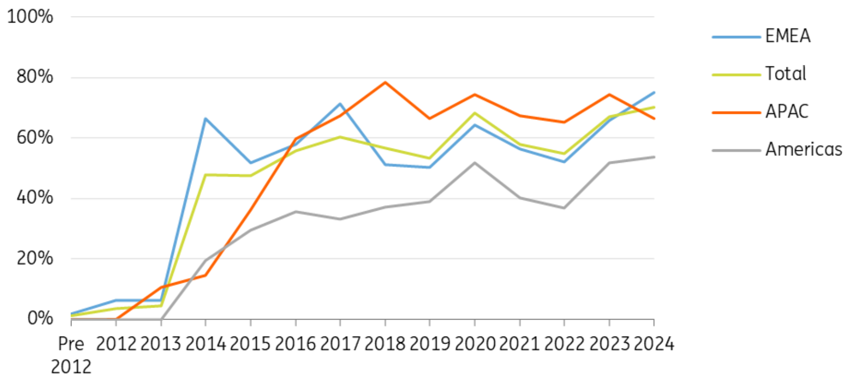
Overall, is there still a greenium? The answer is yes, but it depends – on the issuer, circumstances, and sometimes the currency of issuance. In the end though, there is no magic formula to achieving a greenium. It typically cannot be guaranteed upfront. Here we've focused on secondary market trading levels. We find that issuers with fewer ESG bonds are more likely to have a greenium in the primary market and potentially in the secondary. And the increased popularity of Social can also affect the evolution of greeniums. Bottom line, the greenium discussion remains relevant.

## Credible issuance more important than ever

The sustainable finance market increasingly favours quality over quantity. Quality is reflected in issuers having ambitious climate goals that are backed with interim targets, concrete transition plans, careful choices of eligible projects or material KPIs, third-party assurance, and reporting of impact on a company's sustainability.

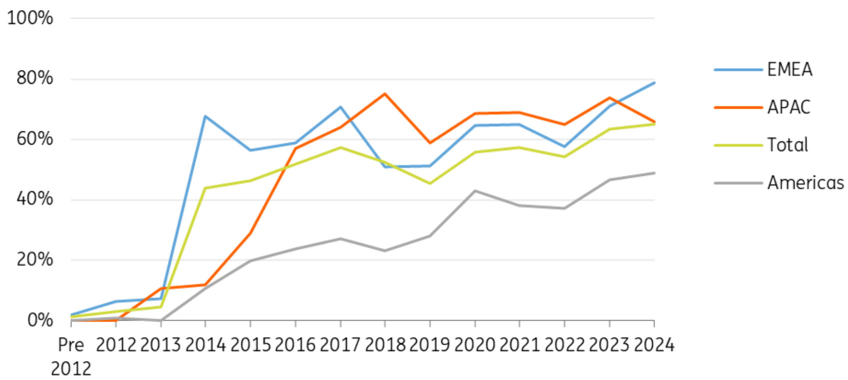
We have seen substantial progress in the past decade. Between 2013 and 2024, the percentage of issuance volumes that are under impact reporting schemes increased from less than 10% to 70%, while the percentage with third-party assurance grew to 65%. There is a clear divide between product types, with bonds much more likely than bonds to have reporting/assurance in place. Looking at geographies, EMEA and APAC are leading and the Americas are lagging. For green bonds, more than 99% of the issuance volume in EMEA has impact reporting and assurance embedded, compared to around 90% in APAC and 70% in the Americas. It is also worth noting that having impact reporting schemes does not mean the reporting is of high quality. Some companies still need to make their reported sustainability data more detailed and consistent.

## Percentage of issuance volumes with impact reporting schemes by region




Data is until 30 June 2024. Source: Bloomberg New Energy Finance, ING Research

## Percentage of issuance volumes with third-party assurance by region




Data is until 30 June 2024. Source: Bloomberg New Energy Finance, ING Research

Mandating sustainability data disclosure can lay a foundation for further quality improvement in sustainable finance, and more and more governments around the world are starting to commit to it.

As of May this year, more than a dozen jurisdictions including China, the UK, Canada, and Brazil had announced plans to adopt the ISSB's sustainability reporting standards. In addition, the EU's Corporate Sustainability Reporting Directive will require approximately 50,000 EU companies and at least 10,000 non-EU companies to disclose a wide range of sustainability data in phases. It is estimated that the jurisdictions committing to incorporating the ISSB or CSRD already account for more than half of the global GDP.

In the US, although the Securities and Exchange Commission (SEC) paused its newly-adopted climate disclosure rule on 4 April amid material legal challenges, California will mandate climate data reporting from large US companies doing business in the state starting from 2026, provided it holds up in court.

Although these mandates differ in disclosure comprehensiveness, strictness, and timeline, they share considerable similarities. Therefore, investors and other stakeholders can expect enhanced sustainability data transparency, comparability, and reliability at the global level in the long term. This would help compare an issuer's sustainable debt impact report with its overall progress toward sustainability. Higher-quality sustainability data can also help issuers set better interim targets and design a more suitable sustainable finance framework.

## Conclusion

The global sustainable finance market is changing for the better. Although issuance is no longer at its peak, it can still be kept at a decent level going forward, given that continuing corporate commitment to sustainability and net-zero emissions needs sustainable debt as a financing tool.

And issuance volume is no longer the only metric the market looks at. Investors and other stakeholders will increasingly search for issuance where material impact can be demonstrated every step of the way. To showcase credibility, issuers are better off adhering to sustainable finance principles not only at a high level but also in detailed operation and reporting. Standard-setting bodies would also benefit from setting more specific guidance on existing or new types of products.

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