Fixed income. Description confusion

Boom in 'sustainable' bonds fuels greater scrutiny of green labels

Many deals fund polluters or projects unrelated to climate as banks chase trillions of dollars

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Troubled waters: Gabon launched the first debt-for-nature swap on the African continent just two weeks before the country's president was ousted in a coup
Amr Abdallah Dalsh/Reuters

Trillion-dollar green finance targets set by leading investment banks are driving a boom in "sustainable" debt deals, many of which have attracted criticism for funding high-emitting companies or financing projects unrelated to environmental goals.

Banks are still working out how to calculate the greenhouse gas emissions linked to their activity financing clients in polluting industries.

They may be forced to start disclosing these emissions in California from 2027 and earlier in the EU and UK, which would increase pressure to cut ties with polluters.

For the moment, banks' climate strategies have focused instead on boosting the volume of lucrative sustainable bond and loan issuance, sparking regulatory scrutiny.

The Financial Conduct Authority in the UK warned bank executives in June over the potential for "greenwashing" in deals that link borrowing costs to sustainability targets.

Marie Jacot-Cardoen, global head of distribution at Edmond de Rothschild Asset Management, said the rapid growth in bonds marketed as sustainable was "positive" for investors looking to diversify their holdings. "But it's like any asset class . . . one has to do the appropriate screening."

Deals that count towards increasingly ubiquitous 2030 sustainable finance targets include those that help oil, gas, coal and shipping companies decarbonise — or that restructure chunks of emerging market debt in exchange for a promise to ringfence a smaller amount of cash for conservation.

Bank of America, which like HSBC has said it aims to mobilise $1tn of sustainable finance by 2030, structured the issuance of $500mn of bonds to investors to fund a general purpose loan to Gabon last month.

This was the first debt-for-nature swap on the African continent and

> 'If they decided to spend all the money on the president's private airplane, so be it'

closed just two weeks before the country's president was ousted in a coup.

The securities were issued by the "Gabon Blue Bond Master Trust" and were described as "blue bonds" in statements to the press by Bank of America.

But in a disclaimer to investors seen by the FT, the bank said it could not guarantee that the description complied with sustainable investing standards.

Its looser definition of the term was contradicted by voluntary market guidance this month from a coalition of UN agencies and the International Capital Markets Association, which represents the biggest players in global bond markets. ICMA said issuers should only add a "blue" marketing label to bonds when all the money is spent on sustainable projects.

Nicholas Pfaff, ICMA's head of sustainable finance, said that, while it did not issue formal labels or guidelines, alternative interpretations of the description could cause "confusion".

He added: "This is a rule we have . . . whether green, blue, social or sustainability bonds, it's 100 per cent [towards the stated project]."

While the "blue bonds" indirectly helped channel money towards marine conservation in Gabon, they lacked a transparent sustainability framework and reporting procedure, and were "not aligned" with market standards, said Daniel Hardy, a researcher at the Vienna Institute for International Economic Research, and former head of the IMF's debt and capital market instruments division.

"If they decided to spend all the money on the president's private airplane, so be it," he said. "If I was an investment manager, I would be concerned I couldn't put this in a green bond portfolio without being sued for false advertising," he added. Bank of America declined to comment.

Banks argue that meeting client demand for the capital needed to transition to cleaner energy production can be a quick and effective way to bring down emissions.

Goldman Sachs, which targets $750bn in sustainable deals between 2019 and 2030, last year said it had reached 55 per cent of this target after just three years.

Deals that counted towards the target include the $3bn acquisition by oil and gas company Chevron of biodiesel maker Renewable Energy Group.

Kara Mangone, head of Goldman Sachs' sustainable finance group, said the bank had "1,000 client meetings" on sustainable financing in the year that it set the target.

Loans to the oil, gas and shipping industry last year that included a variable interest rate based on sustainability goals hit $17.5bn, according to data compiled by European law firm Fieldfisher, similar to $17.7bn the previous year.

Gunvor, one of the world's largest energy traders, obtained an expanded sustainability-linked revolving credit facility totalling $1.125bn from 26 banks in July, including European banks Natixis and Société Générale.

Trafigura, another oil trading giant, refinanced and extended a $5.4bn revolving credit facility in March.

Both traders were promised a lower cost of capital if they could hit certain sustainability targets such as human rights issues or emissions they are directly responsible for.

But the targets did not require them to cut the biggest chunk of their carbon footprint: emissions linked to the consumption of the oil and gas they trade.

Trafigura said the targets in its loans related to "material" business issues. Gunvor said its own loan targets were linked to emissions that the company could "directly influence".

The rapid spread of sustainable finance into more polluting industries is "messy . . . as you can achieve certain targets while hypothetically failing on everything else," according to Jamie Strauss, founder of an environmental, social and governance risk disclosure platform for the mining industry. But he added that it could also help improve governance standards and challenge the idea that all fossil fuel production is "evil".

Australia's Port of Newcastle, the world's largest coal export terminal, whose credit rating was downgraded to junk status by S&P last week, has much of its outstanding debt tied up in sustainability-linked loans pegged to improvements in its carbon emissions.

Its chief executive, Craig Carmody, said that the port's coal export volumes have been declining.

Around three-quarters of the sustainability-linked bonds assessed by the non-profit Climate Bonds Initiative do not "cut the mustard" in terms of quality, according to its chief executive Sean Kidney.

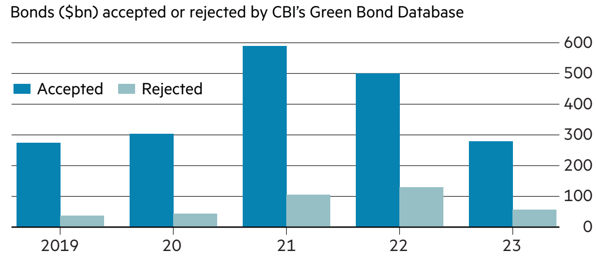
While there are fewer quality problems in green bonds, which earmark proceeds for specific climate-linked projects and make up the majority of the market, the CBI still encounters some that finance coal or gas power plants without a clear transition plan.

Paddy McCully, an analyst at sustainable investment non-profit Reclaim Finance, said he was "hugely sceptical" of banks' sustainable financing targets, which "figure out which direction the market is going in and creatively call it green finance".

He added: "Banks have got to keep all the dregs and nonsense out of their sustainable finance, otherwise they risk diluting the amount of money that goes towards genuinely green projects."

More bonds are being rejected because of quality concerns

Bonds ($bn) accepted or rejected by CBI's Green Bond Database



2023=first half; figures are for bonds described as green by issuers
Source: Climate Bonds Initiative