Zuger Kantonalbank

ESG at Zuger Kantonalbank

# Bonds with a sustainability focus

**We are conscious of our responsibility towards the environment, society and future generations. With a holistic approach, we are committed to underpinning our business with ethical principles as well as social and environmental responsibilities, thereby fostering sustainable and beneficial development. By doing so we create added value – for our stakeholder groups and for the environment.**

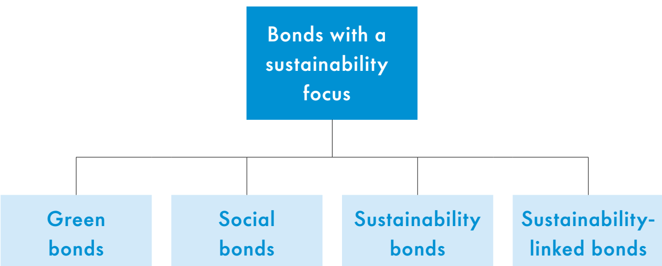
## From niche product to market segment

The first bonds with a sustainability focus were issued in 2007 (in the form of green bonds) by the European Investment Bank (EIB) and the World Bank. On the one hand, the aim was to raise capital for environmentally friendly projects and, on the other hand, to offer investors an instrument that takes this goal into account. Originally launched as niche products, bonds with a sustainability focus now account for a significant share of the international financial markets.

> The intended use of a bond with a sustainability focus is precisely defined and usually linked to ecological and/or social projects. Moreover, these bonds have similar characteristics and yields to traditional bonds.

## Different structures

A bond with a sustainability focus is a fixed-income investment issued by corporations, governments, or other organisations to raise capital specifically for projects or initiatives that have a positive environmental or social impact. These bonds are intended to support clearly defined sustainability goals. Strict guidelines and voluntary certifications (such as that of the International Capital Market Association, ICMA) are intended to prevent greenwashing. In contrast to conventional bonds, with bonds with a sustainability focus investors are assured that their money will only be used for responsible projects. In addition to the earmarked use of funds, compliance with standards and reporting are other key elements. This ensures that the bonds actually meet sustainable criteria and that investors are transparently informed about the performance. Within the group of bonds with a sustainability focus, a distinction is made between the following categories:




**Green bonds** are issued specifically to finance projects with a positive environmental impact, such as renewable energies or energy efficiency measures. Climate bonds are a subset of green bonds. They focus exclusively on projects that deal with adaptation to climate change or with climate protection.

**Social bonds** are similar in design to green bonds, but finance projects that contribute to social sustainability (e.g. access to basic services, social housing or educational initiatives).

**Sustainability bonds** are a mix of green bonds and social bonds, i.e. the money is used exclusively to finance a combination of environmental and social projects.

**Sustainability-linked bonds (SLBs)** are all types of bonds whose financial or structural characteristics may vary. These are subject to the condition that the issuer achieves the predefined sustainability goals. Issuers thus expressly commit to make future improvements in sustainability results within a predefined time frame. SLBs are a forward-looking, performance-based instrument.

| | Traditional bonds | Bonds with a sustainability focus |
|---|---|---|
| **Structure** | Debt instruments for which the issuer promises to make regular interest payments to the investor and to repay the nominal value at maturity. | |
| **Risk** | Credit risk (possibility of the issuer becoming insolvent) and interest rate risk (possibility of the market interest rates and the value of the bond changing). | |
| **Investors** | Both types of bonds can be purchased by institutional and private investors. | |
| **Types of use** | Capital for general corporate purposes or government spending without specific sustainability goals. | Exclusive financing of projects that have a positive environmental or social impact. |
| **Valuation** | Valuation is mainly based on financial key figures and the creditworthiness of the issuer. | In addition to financial criteria, ESG factors are also taken into account. |
| **Yields** | Yield is mainly based on general market conditions and the creditworthiness of the issuer. | Comparable, possibly lower financial returns in exchange for positive social or environmental impact. |

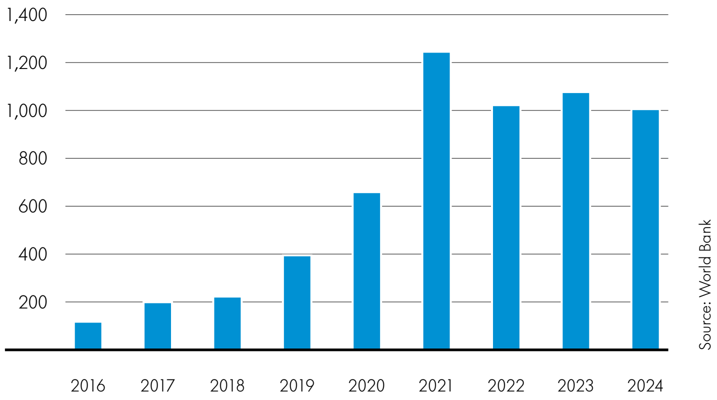
## Issuance trend

The European Investment Bank (EIB) pioneered the green bond market in 2007 with its Climate Awareness Bond. In the early years, interest in sustainable bonds remained very manageable and was almost exclusively covered by supranational organisations. It was only in 2014 when the International Capital Market Association (ICMA) published its set of rules – the "Green Bond Principles" which still play a leading role to this day – that demand slowly increased. From 2015, it received further support due to the ratification of the Paris Climate Agreement. In addition to green bonds, social bonds and sustainability bonds have become more important with the formulation of the 17 United Nations Sustainable Development Goals. Moreover, companies have also discovered this financing option for themselves. Since the launch in 2007, the global issuance of bonds with a sustainability focus has grown significantly every year and reached USD 1,200 billion in 2021. The increase from 2020 to 2021 – the result of an above-average number of social bonds issued to tackle the financial aspects of the Covid-19 crisis – is particularly striking. From 2022, issuing activity was again somewhat lower, which was also due to factors such as the war in Ukraine or the development of inflation. However, issues running into the billions show that interest in bonds with a sustainability focus remains high.

## Greenium

The term "greenium" describes the price premium (or yield discount) that investors are willing to pay for green or sustainable financial products compared to conventional bonds of the same creditworthiness and maturity. This key figure has changed markedly in recent years, however. In Switzerland and also globally, the greenium is now close to zero, which means that investors receive the sustainable added value almost at zero cost. This is partly due to the fact that the supply of bonds with a sustainability focus is steadily growing, which reduces the price premium.

**Issuance of sustainability bonds (USD bn)**




## What does this mean for investors?

Bonds with a sustainability focus thus have similar characteristics and yields to traditional bonds. Investors who want to participate in the fixed-income sector while also ensuring that their investment is used exclusively for sustainable purposes therefore prefer this type of bond. For further information on our investment solutions, please contact your Zuger Kantonalbank advisor.

## Publications

Other publications on the subject of ESG can be found on our web page www.zugerkb.ch/en/esg.

Zuger Kantonalbank

**We are signatories to or members of the following organisations**

Signatory of: PRI Principles for Responsible Investment

Swiss Sustainable Finance

ASSET MANAGEMENT ASSOCIATION

**Contact**
esg-investments@zugerkb.ch