BEYOND COMPLIANCE

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Green Bond vs Sustainability Bond

Green bonds are issued by institutions to fund projects that have positive environmental and/or climate benefits. Proceeds from these bonds must be used for "green" projects.

Sustainability bonds, then, are issued to fund projects that have a positive social or governance benefit. So, for example, a green bond would be issued by an institution to fund installation of solar panels. On the other hand, a sustainability bond would be issued to fund a project aimed to address gender equality.

These bonds are regulated instruments subject to the same capital market and financial regulation as other listed fixed income securities.

The Green Bond Principles (GBP) and Sustainability Bond Guidelines (SBG) have become the leading framework globally for issuance of green and sustainability bonds.

Sustainable Finance – The Bottom Line

Economics is the study of how societies use scarce resources to produce valuable commodities and distribute them among different groups. There is a finite amount of financial resources available and each group within an organization is vying for what they believe should be their share.

How then, can we influence organizations to make financial decisions and provide resources for projects that have positive environmental, social and governance (ESG) benefits?

Today, there are three important factors that are driving how finance affects decision-making around sustainable business practices:

- It simply costs too much
- Investing in companies with good business practices is good business
- Investors are using their influence and cash to drive positive change

It Simply Costs Too Much. There are two types of internal investments that a company can make with regard to increasing sustainable outcomes – controlling operational costs and capital expenditure strategies. For example, reducing waste generation and energy use has a positive impact on the bottom line. These actions will reduce operational costs and may be achieved without having to make a capital expenditure.

However, looking at return on investment (ROI) as the sole decision factor for a capital expenditure will typically not give preferentiality to sustainable projects. "The main function of capital is to grow the business, not principally to reduce operational costs." - Zach Masdorf, EHS Today. The company must look at a multitude of factors, including ROI, when making a decision regarding capital expenditures with respect to sustainability. This is where the influence of your stakeholders comes into play. A true cost-benefit analysis could be used as an alternative or supplement, which would factor in many of the "softer" benefits that result from sustainability or "green" projects.

About the Author

Donna Switzer is the founder of Beyond Compliance LLC Consulting of the Greater Philadelphia Area, a woman-owned sustainability and environmental, health and safety (EHS) consulting firm that partners with organizations to solve regulatory compliance requirements. Donna is passionate about reducing risks associated with air emissions, wastewater discharges, waste management, and workplace safety. She has worked with a broad range of organizations in chemical, pharmaceutical, manufacturing, construction, and power sectors in developing, implementing, and evaluating key sustainability and EHS programs.

Donna is an Adjunct Professor at Villanova University and holds the following certifications: Certified Sustainability Practitioner, Certified Professional Environmental Auditor, and Certified Hazardous Materials Manager.

Capital expenditure projects having benefits that meet multiple corporate requirements have a better chance of being implemented, even if the ROI is not as favorable. Additionally, comparing operational costs and other externalities between two capital project alternatives may prove that the sustainable option is the best choice.

Investing in companies with good business practices is good business. A well-run company that thoughtfully calculates risks and implements controls is more likely be continually successful than a company whose sole purpose is to make a bigger profit. "Sustainable companies are earning increased gains because they focus on things that aided their businesses, like wasting less water and energy, incentivizing their CEOs to focus on the long term and providing high-quality, diverse workplaces that lead to greater employee satisfaction, retention and productivity." - Audrey Choi, Morgan Stanley Chief Marketing Officer & Chief Sustainability Officer. There are many methods by which financial institutions rate company performance. Some methods are unreliable or are developed without your input. Three examples include the Dow Jones Sustainability Index, CSR Hub, and the Bloomberg Terminal. These organizations collect available information about your company and provide an opinion about your performance. Investors then use that information to make investment decisions.

Investors are using their influence and their cash to drive positive change. As social issues become more important to young executives and decision makers, their investments will shift to reflect their personal beliefs, whereby avoiding investment in companies associated with addictive behavior like tobacco and gambling, and focusing on companies associated with social justice and environmental performance.

"As the global population increases to 9.7 billion in 2050 and the strain on available food, water, and energy resources grows exponentially, I believe that the nearly $300 trillion worth of stocks, bonds and other investments in the marketplace can be one of the most powerful forces for positive social change to meet those needs." - Audrey Choi, Morgan Stanley Chief Marketing Officer & Chief Sustainability Officer. In a 2018 study, the Harvard Kennedy School reports that socially responsible investing now accounts for 26 trillion USD. Environmental-finance.com reports that ESG bond issuance has gone from less than 50 trillion USD in 2015 to more than 200 trillion USD in 2018.

In conclusion…

We all know that financial resources drive decision making. Increasingly, investors are making "greener" decisions by seeking ESG information about their investments. Looking at ROI as the sole decisive factor for a capital expenditure may be too short-sighted for your stakeholders. Studies show that there is an increase in funds provided for projects with ESG benefits.

If you would like more information about how you can plan for and implement a successful sustainability program, please contact us.

Resources:

Photo by Shopify Partners from Burst
Morgan Stanley Wealth Management Article
Harvard Study
EHSToday
CSR Hub, DJSI, and the Bloomberg Terminal
Environmental-Finance.com

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