

# The Treasury

## New Zealand Sovereign Green Bonds Programme Information Release

November 2022

This document has been proactively released by the Treasury/Minister of Finance (Hon Grant Robertson) on the Treasury website at

<https://treasury.govt.nz/publications/information-release/new-zealand-sovereign-green-bonds-programme>

### Information Withheld

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act).

Where this is the case, the relevant sections of the Act that would apply have been identified.

Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to sections of the Act under which information has been withheld:

- [34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions
- [35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment
- [37] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice
- [39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [34] appearing where information has been withheld in a release document refers to section 9(2)(g)(i).

### Copyright and Licensing

Cabinet material and advice to Ministers from the Treasury and other public service departments are © **Crown copyright** but are licensed for re-use under **Creative Commons Attribution 4.0 International (CC BY 4.0)** [<https://creativecommons.org/licenses/by/4.0/>].

For material created by other parties, copyright is held by them and they must be consulted on the licensing terms that they apply to their material.

### Accessibility

The Treasury can provide an alternate HTML version of this material if requested. Please cite this document's title or PDF file name when you email a request to [information@treasury.govt.nz](mailto:information@treasury.govt.nz).

Reference: T2021/2352

File No. DE-3-0-13



Date: 16 September 2021

To: Minister of Finance (Hon Grant Robertson)

Deadline: None

## **Aide Memoire: New Zealand Labelled Bond Update**

The purpose of this Aide Memoire is to:

- Update you on work underway within the Treasury on a potential labelled bond programme (LBP). The Treasury are considering several potential options, including 'green' or 'sustainable' bonds.
- Highlight links between the LBP and the broader advice you are due to receive on climate funding and financing.

We will be providing more substantive advice on an LBP in late September 2021. The Treasury considers there are benefits in establishing an LBP, and that advice will seek your in-principle agreement to proceed in doing so. Should you proceed, you have options available to you around the timing of an announcement, including at the 2021 United Nations Climate Change Conference (COP 26) or through the Emissions Reduction Plan.

### **Work underway on labelled bonds**

The Treasury is progressing its review of labelled bond options. This section sets out what an LBP might look like and summarises high-level benefits and risks. This content broadly follows that provided to you in a slide pack on 19 August 2021 [T20201/2145 refers].

#### ***What is a labelled bond programme?***

An LBP establishes a framework for issuing labelled bonds (for example 'green', 'social', or 'sustainable' bonds). A framework typically involves four elements:

1. Use of proceeds determination.
2. Project evaluation and selection in line with eligibility criteria. Projects must have specific and dedicated environmental and/or social benefits.
3. Management of proceeds, ensuring LBP proceeds are appropriately allocated, and
4. Reporting, including tracking of proceeds and impact reporting.

There are globally established precedents for these frameworks, including external assurance and certification.<sup>1</sup> Following best practice is necessary for investor confidence in the credibility of the LBP.

Beyond the framework identified above, a labelled bond is similar to a generic New Zealand Government Bond (NZGB). An LBP would not provide any additional fiscal headroom relative to the current approach of issuing NZGBs. As happens now, the size of your borrowing programme would be set with reference to your fiscal strategy. Assuming equivalent bond pricing and tenor, the fiscal impacts of an LBP would be identical in all respects to equivalent NZGBs – including how they affect core Crown net debt and OBEGAL.

### ***What is the case for a labelled bond programme?***

An LBP offers potential benefits relative to the Treasury's debt management objectives. These include:

- Diversification of the investor base – which reduces the risk of changes in investor demand from segments of investors undesirably affecting the Crown's finance costs, and
- Supporting New Zealand's capital markets development, especially if a "Sustainable/Green curve" is able to be established. The NZGB yield curve provides a benchmark for other debt issuers. A sovereign sustainable/green curve could likewise provide a benchmark for debt market issuers with labelled bond debt products.

An LBP may also provide broader benefits beyond debt management:

- An LBP could potentially provide additional discipline and transparency to the Crown's capital investment pipeline, including supporting alignment with the Government's climate objectives. The impact of qualifying projects must be demonstrated before they can meet eligibility criteria for the LBP. This involves rigorous reporting requirements and external review (this may be both prior to and after issuance). There are already a range of reporting requirements in New Zealand's investment management system, but an LBP may strengthen these requirements. The presence of external investors means there are additional reputational consequences for a failure to report.
- Linked to above, an LBP may assist in the development of the investment pipeline (particularly if agencies consider they are more likely to receive funding from meeting LBP requirements).
- 'Shining a light' on the NZ government's climate related work and commitments.

### ***What are the risks and challenges?***

Risks and challenges include:

- Reporting requirements have cost. Rigorous reporting requirements can be both expensive and time intensive. Agencies responsible for qualifying projects will need to support reporting requirements and Treasury will need to coordinate this reporting activity.

---

<sup>1</sup> In the case of the UK's Green Gilt programme for example, the UK Government sought a review of the framework against the ICMA Green Bond Principles, and also sought a pre-issuance report comparing the use of proceeds to the UK's carbon budget.

- Investment will be required in structures to meet project selection, monitoring and reporting requirements. It will take time to set up these structures. For this reason, it is likely to be efficient to use existing structures where possible (for example the Capital Investment Committee).
- Identification of qualifying projects. A key precursor to an LBP is sufficient volume of qualifying projects to support an issuance programme that has material and sustainable volume. Although we are confident the pipeline of eligible projects will be large, given the range of climate related programmes being considered across the Crown, there will be shorter-term challenges in building a pipeline and ensuring we have sufficient capacity in place to ensure delivery.
- The large volume of tasks to be completed in a short period of time, if we were to target a programme announcement later this year, with an intention to issue our first labelled bonds in the second half of calendar 2022.
- Without cross departmental co-operation, additional expenditure and improvements in discipline and reporting there is a risk that there may be limited improvement in environmental outcomes.
- Investor demand and bond markets may evolve to take a whole-of-government view of expenditure, impacting the longevity of the labelled bonds market.

## Link to climate funding and financing

### ***How does a labelled bond fit into the broader work taking place on climate funding and financing?***

The Treasury and MfE have been leading a work programme that considers options for funding and financing the climate transition. Through the work programme, we understand that you will receive advice covering four focus areas:

1. Hypothecation of ETS revenues
2. Design of the Climate Emergency Response Fund (CERF)
3. Exploring a role for co-investment institutions, and
4. Developing tools to monitor, track, and align climate spending.

In our view, the case for an LBP is not contingent on decisions in any of these four areas. There will nonetheless be opportunities to consider how an LBP can complement the work programme:

- *ETS hypothecation*: we would not see labelled bonds as being ringfenced to be repaid directly by hypothecated ETS revenue (this would negatively impact bond pricing, given the challenge in forecasting this revenue and additional risk). Instead, the bonds would be repaid from general Crown revenue. The Crown would have options in how it internally accounted for these revenues, however, and Ministers may have interest in using financing to 'bring forward' ETS revenue to match the desired expenditure profile.
- [34], [37]

---

<sup>2</sup> [34], [37]

- *Co-Investment Institutions:* financing from the labelled bond could potentially be provided to an institution, subject to the institution meeting Eligible Expenditure, monitoring and reporting requirements. The Treasury considers there are benefits to issuance occurring centrally, rather than the institution raising the financing from its own balance sheet, including:
  - Lower cost. Any government agency borrowing off their own balance sheet will pay a margin above New Zealand Government Bonds (NZGBs) that the Treasury do not consider reflects a genuine transfer of risk to investors in the capital markets. The government agency would also need to establish and maintain their own treasury function.
  - Centralisation more effectively allows the Government to demonstrate market leadership and provide support for New Zealand’s capital markets development, especially if a ‘sustainability curve’ is able to be established.
  - A centralised programme provides a stronger statement in relation to the Government’s climate commitments, and can be more closely aligned with other Government responses, such as the ERP.
  - In order for the LBP and its bonds to be liquid, relevant, enduring and credible, it needs to have a large volume of Eligible Expenditure incorporated within it. Direct market issuance by other government agencies will reduce the pool of projects available to the LBP.
  - The Crown has more ability than agencies to manage the balance between labelled bonds and other sources of financing in its borrowing programme.
- *Tools to track and monitor:* Both the LBP and CERF will require tools to track and monitor spending. We will consider any efficiencies between tools Officials are considering for CERF and the LBP framework requirements.

### ***A case study: Waka Kotahi and labelled bonds***

You recently agreed to consider providing Waka Kotahi with a financing facility of up to \$2 billion. In our supporting advice, we noted that “agreeing to establish a financing facility does not preclude the inclusion of Waka Kotahi projects in a green or sustainable bond programme managed by the Treasury” [T2021/2088 refers]. How would that work in practice? In short:

- The Crown would issue bonds under an LBP, administered by the Treasury’s Debt Management. The proceeds of that issuance would be used to fund Waka Kotahi projects that met eligibility criteria for the LBP. Our indicative analysis suggests several significant projects would qualify (for example public transport infrastructure).
- Waka Kotahi would provide the Treasury with any reporting required for us to meet our obligations under the LBP.
- A separate financing facility would be agreed between the Treasury and Waka Kotahi, providing for repayment of funds raised through the LBP. The use of debt reflects the beneficiary pays nature of the National Land Transport Fund: for other

forms of capital investment (e.g. social infrastructure) proceeds from the LBP may be provided in the form of grants.

### ***How do decisions around the labelled bond programme link to the ERP?***

The Emissions Reduction Plan (ERP) will necessitate significant climate related expenditure over an extended period. The LBP could ensure a spotlight is shone on key projects and that they are actively monitored, ensuring impacts of those projects are well considered and achieved.

### **Next Steps**

The Treasury will provide further advice on the labelled bond programme by the end of September and seek formal approval to proceed with establishing the programme. The advice will cover:

- Description of how the LBP is envisioned to work
- Milestone timeline
- Initial estimate of costs, and
- What needs to be achieved ahead of a public announcement.

We note that while many decisions regarding an LBP sit with you as Minister of Finance, we would recommend socialising those decisions with your Cabinet colleagues, particularly given potential impacts on reporting requirements for the Crown's capital investment pipeline. We will set out options to do so in our timeline.

A target date for public announcement of the programme will help us manage our workflows. Our preference is to have a public announcement made by early November. A public announcement will allow us to proceed with engaging with the multiple internal and external parties expected to be involved in the project. Proceeding with external engagement before announcement may risk frontrunning any announcements Ministers may wish to make. Early November may line up well with COP26, however we appreciate you may have your own views on timing.

Given links to the work on climate funding and financing, you may wish to share this Aide-Memoire with the Minister for Climate Change.

**Karina Witty**, Senior Funding and Engagement Strategist, Capital Markets Funding Strategy and Engagement, [39]

**Alistair Birchall**, Manager, Capital Markets Policy, [39]

**Kim Martin**, Head of Funding Strategy and Engagement, Capital Markets Funding Strategy and Engagement, +64 4 890 7274