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Asia-Pac companies sold US$124.53b of green bonds in 2021, up from US$54b in 2020, but those that fail to adapt will see smaller pools of capital, higher funding costs

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GREEN bonds are set to be the fastest-growing segment in Asia's debt markets in 2022, but borrowers can expect to face greater scrutiny – not just from lenders and investors, but also governments and regulators – which means those that fail to adapt will see smaller pools of capital and face higher funding costs, experts say.

"For polluting entities that decline to curb emissions, lenders and investors are walking away, governments are getting involved, and regulators are stepping in," said Charles Chang, S&P Global Ratings' Greater China Country Lead for corporates.

Investors are increasingly differentiating among sectors, Howard Chu, head of APAC Fixed Income Syndicate at JP Morgan, said. While some investors are very "black and white" in that they want nothing to do with coal, others have broader mandates, such as credit funds or hedge funds, and may be open to looking at some of the traditional dirtier industries, focusing on their ESG plans, initiatives and commitment to decarbonisation.

Environmental, social and governance (ESG) regulation in Asia Pacific is accelerating – a reality that all asset managers and corporates must face.

"Accompanying this are new, material cost considerations and an urgent need for up-skilling by investors and corporates, as well as potential valuation implications for stocks based on levels of alignment with developing ESG standards," Goldman experts said.

Global sales of green bonds – debt used to fund environment and climate related projects – reached a record level of almost US$474 billion in 2021, up from US$296 billion in 2020, according to data by the Climate Bonds Initiative, or CBI.

Asia Pacific was the biggest growth region, where companies sold US$124.53 billion of green bonds in 2021, up from US$54 billion in 2020. Next was Europe, where issuance jumped to US$240 billion, from US$157 billion.

Non-financial corporations globally supplied US$141 billion of bonds last year, from $76 billion a year earlier. The data covers bonds aligned with CBI definitions. Another US$55.31 billion of green bonds issued globally in 2021 were reported by the CBI as non-aligned, while US$95.39 billion have not yet been categorised.

Regional companies that are aligned with the European Union's green taxonomies trade at premiums of 55 per cent price to equity (PE) and 64 per cent enterprise value over earning before interest, tax, depreciation and amortisation (EV/Ebitda). These compare to green premiums of 37 per cent globally. Goldman said the region's higher premiums reflect the high concentration of electric vehicle and battery related stocks as well as upstream solar equipment manufacturers.

New and emerging ESG fund requirements are seen in Hong Kong, Malaysia, Taiwan, Australia, India, Japan, New Zealand, Singapore, Thailand, and Asean requiring asset managers to disclose how ESG is integrated into the investment process or setting minimum fund investment thresholds in "ESG" stocks.

Bertrand Jabouley, head of Sustainable Finance, Asia-Pacific, S&P Global Ratings, said: "Investors want to see financing frameworks abide by established standards from well-known bodies. These bodies are tightening the screws and making compliance with their standards more demanding."

However, criteria shifts, data inadequacies, governance shortfalls, and human resource constraints continue to make selection challenging for investors.

"They find it particularly difficult to measure the green performance of these new financial instruments," Chang said.

Dave Fernandez, director, Sim Kee Boon Institute for Financial Economics & co-director, Singapore Green Finance Centre at Singapore Management University, noted that end-investors do not discriminate between the greenwashers and genuinely green funds.

"More than 90 per cent of the world's largest companies produce corporate social responsibility reports, but third parties review only a minority of these," he said. "There are valid concerns about the reliability of such self-reporting. The bottom line is that we'll likely see regulators step up in this area."

The global ESG standards launch this year, developed by the International Sustainability Standards Board (ISSB), should improve corporate disclosure across the region .

Goldman said as investors access more ESG data, the focus should be on measuring actual performance rather than disclosure alone: "We find consistent links between ESG metrics and return on capital, which have a large divergence in outcomes when analysing ESG performance versus disclosure-based scoring approaches."