



Sustainable Finance Bulletin

03

DZ BANK Spotlight:

Sustainable Bond market forecast 2020

Welcome to the decade of Sustainable Finance. We are entering a new age for finance. We are in a sustainability investment race; to attract the trillions in private capital needed for the sustainable transformation.

The global fixed income market plays a key role in this transformation process. With an estimated volume of more than 100 trillion US Dollar, it bears huge potential for facilitating the transition to a sustainable future.

2019: a record year for Sustainable Bonds

For the first time in the history of the Green Bond market the new issue volume already broke through the USD 100 billion mark in the first half of the year. On 17 September 2019 new issue volume of Green Bonds surpassed 2018 total issuance and on 21 October 2019 it exceeded the USD 200bn mark for the first time. Overall, 2019 issuance increased by 51% compared to the previous year to USD 257.7bn (2018: USD 170.6bn), hence surpassing our forecast of USD 225bn.

Market diversification, described by us as „Green goes rainbow“, continued in 2019. Issuers and investors are increasingly looking beyond the pure environmental perspective.

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Dear Reader,

Welcome to the decade of Sustainable Finance.

We are pleased to present the latest edition of our Sustainable Finance Bulletin.

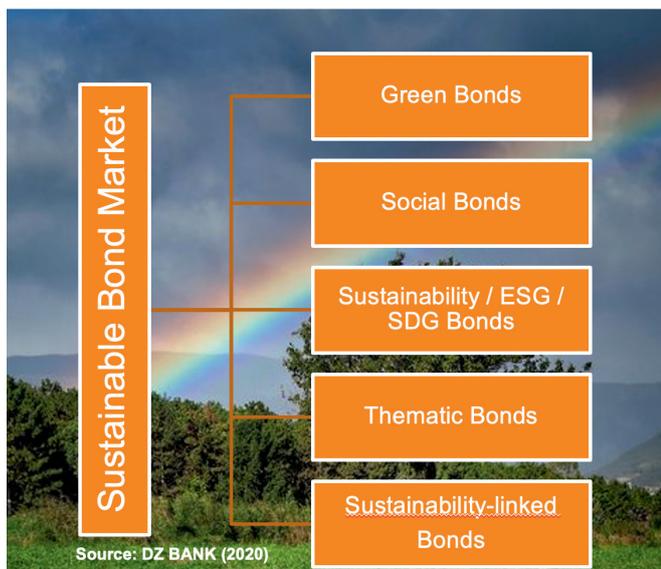
The role of the financial sector in transforming our economy and society towards sustainability had been overlooked for too long. Fortunately, capital markets have started to take the right path to support this transformation. Some years ago, sustainable finance used to be a small niche. But today it is becoming a transformational force.

Enjoy reading!

Marcus Pratsch

Head of Sustainable Bonds & Finance

The market is becoming „more colourful“. While new issue volume of social bonds rose by around 41% to USD 20 billion (2018: USD 14.2 billion), ESG, Sustainability and SDG Bonds in particular proved to be the market’s growth drivers, with the volume of new issues tripling to USD 65 billion (2018: USD 21 billion).



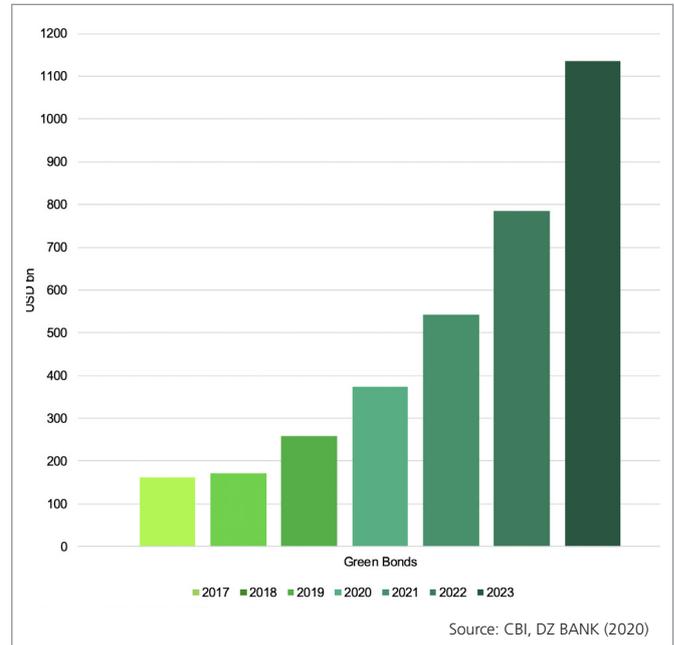
“Green goes rainbow”: Sustainable Bond Classification

New labels such as Transition Bonds (MARFRIG Global Foods) and Sustainability-linked Bonds (Enel’s SDG-linked Bond) saw the light of day. In addition, the market came up with a number of innovative approaches, such as DKB’s Blue Social Pfandbrief.

The 2020s: the decade of Sustainable Bonds

2020 marks the beginning of a decade of urgent climate and sustainability action. Sustainability will become a decisive factor in business. Hence, we expect strong pick-up in investor demand for Sustainable Bonds.

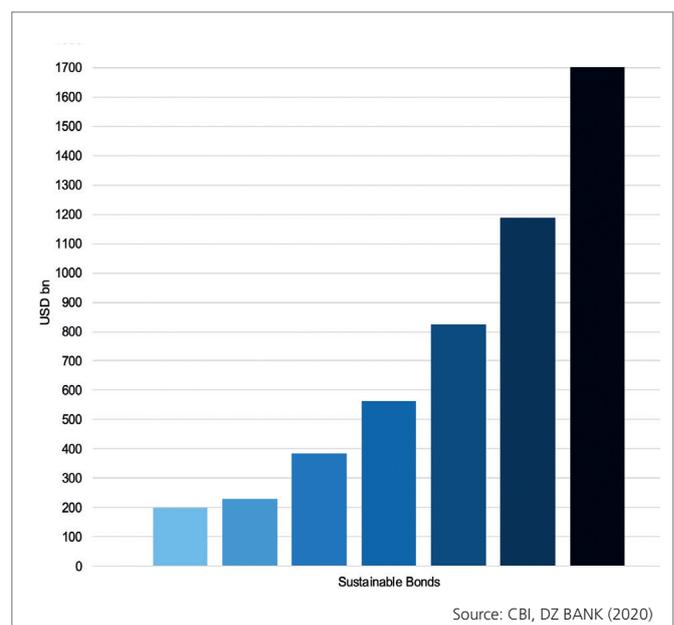
We expect the Green Bond market to grow in 2020 by around 45% to USD 375bn, hence exceeding the USD 300bn mark for the first time. Sovereign Green Bonds will be one of the key growth drivers of the segment. Sovereigns like Germany, Austria, Italy, Spain and Sweden are expected to debut on the Green Bond market while countries like France and the Netherlands are expected to come to the market again.



Green Bond Market Forecast

The diversification of the market will continue in 2020 and subsequent years. Especially with regard to the Sustainable Development Goals, we see huge potential for the Corporate Sustainable Bond market in the DACH region. In Germany, for example, no non-financial corporate has yet issued a benchmark Social or Sustainability Bond.

We forecast new issuance in the total global Sustainable Bond market to grow by around 47% to approx. USD 560bn, hence exceeding the USD 500bn mark (“halfway to the trillion”) for the first time.



Sustainable Bond Market Forecast

We are expecting to exceed the critical 1 trillion US-Dollar mark in the total Sustainable Bond market by the end of 2022. The Green Bond market will most likely see the first trillion in annual issuance by the end 2023.



“Leaving no one behind”

Guest Commentary: Green Banking is on the rise in the real estate sector



Dirk Schönfeld,
Head of Treasury,
Deutsche Hypo

The issue of sustainability has been much discussed for some years now – not least because of the consequences of climate change, which are already being felt today. In addition to the own self-image towards a conscious, serious organisation, it is also the changed expectations of customers, investors, owners, rating agencies or the public that make a holistically sustainable positioning of a company necessary. As a result, corporate social responsibility (CSR) has become an integral part of the bank’s corporate management, and has also become an integral part of the real estate financing industry. As a German real estate bank with a European focus, Deutsche Hypo actively supports its customers in the spatial design of many cities. „We have taken this as an opportunity to make a sustainable contribution to the future of our cities in our core business“, emphasises Sabine Barthauer, Member of the Board of Managing Directors of Deutsche Hypo. Sustainability is therefore not a one-off action, but a process of continuous development

of the bank. Consequently, it requires a link to the actual core business. For some years now, Deutsche Hypo has been working on the sustainable organisation of its business model and introduced a professional sustainability management for this purpose in 2013. In connection with this, a sustainability strategy was developed which complements the business strategy. „A particular focus is on systematically reducing the environmental impact of our business activities,“ states Sabine Barthauer. By saving resources, energy and emissions, the bank’s eco-efficiency is continually being improved.

Since 2017, Deutsche Hypo has consistently transferred the issue of sustainability to the banking business and has created a green value chain with two new products for the assets and liabilities side of the balance sheet: Green Bonds and Green Loans. Green bonds are issued in the form of green Pfandbriefe, which are based on financing for energy-efficient buildings. All funds raised through the issue will be used exclusively for the financing of energy-efficient buildings according to the so-called „Use of Proceeds“ principle. Green Loans, in which Deutsche Hypo offers its customers an interest rate advantage for financing energy-efficient buildings, are therefore a logical development. An energy-efficient building, also known as a „Green Building“, is a building that is modern, contemporary and as future-oriented as possible. In addition, it has a good to very good location for the specific type of use and is particularly energy-efficient due to modern systems engineering and its very good energy properties. However, it is not only about the building structure, but also about traffic and usage concepts.

The trend towards green financial products continues to grow among investors and borrowers. „We are noticing an increased demand for green financial products, which we are very happy to meet,“ explains Sabine Barthauer. This gives the Deutsche Hypo the opportunity to broaden its investor base. The disproportionately high demand for sustainable properties also leads to lower-risk financing. „We can encourage customers to consider the topic of resource conservation as well as sustainable and environmentally conscious construction. In addition, our know-how provides added value for customers and investors,“ asserts Sabine Barthauer. „For years we have been experiencing a social change towards a sustainable consciousness, the pace of which has increased significantly, not least due to the „Fridays for future“ movement. Even though we at Deutsche Hypo have already implemented a number of measures in this direction, we too are on a path that we will resolutely continue to follow“.

DZ BANK Spotlight: Sustainability-linked Bonds

The emergence of new labels in the sustainable fixed income world sparked controversies among investors in 2019.

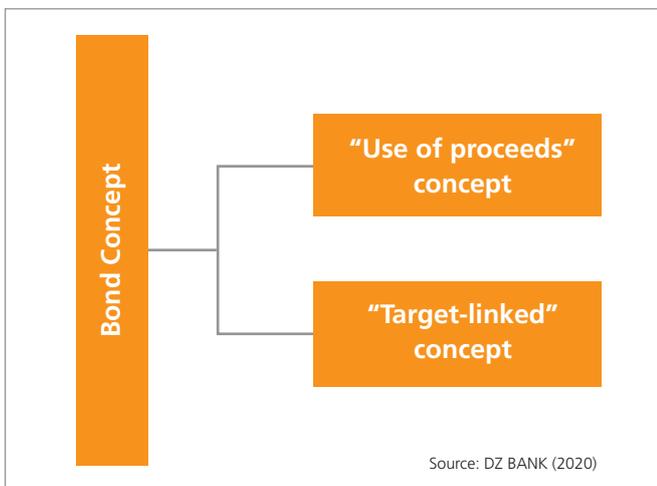
One of the labels that stood in the crossfire were Sustainability-linked Bonds, which allow for more outcome-focused sustainable finance. The criticism from some investors focuses on the fact that the issuer will be free to spend use of proceeds from Sustainability-linked Bonds, i.e. without being tied to a sustainable purpose.

While proceeds from traditional Sustainable Bonds (Green Bonds, Social Bonds and Sustainability Bonds) must be earmarked for sustainable projects according to ICMA standards (so-called "use of proceeds" variant), Sustainability-linked Bonds are non-earmarked standard bonds whose financing cost may be increased in the event of failure to achieve a sustainable performance objective (so-called "target-linked" variant). The interest rate can move up or down depending on performance relative to selected KPIs or a sustainability rating.

In addition, by entering into such financing arrangements, issuers also run a reputational risk if they fail to meet their targets, i.e. there is no improvement with regard to the KPIs or the sustainability rating.

Finally yet importantly, Sustainability-linked Bonds offer sustainability-oriented investors a wider range of investment opportunities.

We forecast that issuing sustainability-linked investment vehicles will continue to grow in importance in 2020. We see especially huge potential for Schuldscheine issued by small and medium-sized corporates. For sustained qualitative growth, however, it is necessary for the segment to achieve a similarly high level of transparency and integrity as the market segment for earmarked bonds („use of proceeds" bonds). Hence, the International Capital Markets Association (ICMA) has recently announced to establish a working group on emerging sustainability/KPI-linked bond products to take stock of recent and ongoing developments in the market for sustainability/KPI-linked bond products and to consider and potentially propose market guidance.



Diversification: allowing outcome-focused Sustainable Finance

However, Sustainability-linked Bonds open sustainable funding opportunities for issuers that so far have been unable to issue traditional Sustainable Bonds because they cannot identify sufficient eligible assets / expenditures connected to sustainability. Issuing target-link structures allows them to contribute to the global sustainable finance agenda by focusing on a broader transformation rather than focusing on specific projects. This especially holds through for a large number of small- and medium-sized corporates. Issuing a Sustainability-linked Schuldschein would be particularly suitable for them.

Save-the-date:

DZ BANK Capital Markets Conference 2020

This year's DZ BANK Capital Markets Conference will take place at the DZ BANK premises in Berlin from 5 to 7 May 2020. It will be organised in cooperation with OMFIF, KfW and Deutsche Bundesbank.

As in previous years, Sustainable Finance will be one of the main topics of numerous discussions.

Information on the event will be updated on an ongoing basis at the following link: <https://live.dzbank.de/cmc/home>

You will soon be able to register. The number of participants will be limited.



The banner features a collage of images on the left, including the DZ BANK logo, a woman using a tablet, the European Union flag, a bull market, a robot hand, the Reichstag dome, the Brandenburg Gate, and a city skyline. The right side has an orange background with white text: 'Save the Date DZ BANK Capital Markets Conference 2020', '5th – 7th May 2020, DZ BANK Berlin', and logos for OMFIF, KfW, and Deutsche Bundesbank Eurosystem. The DZ BANK logo is at the bottom right.

LEGAL REFERENCES

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