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Nordic public sector roundtable

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Nordic public sector borrowers benefit from safe haven status and funding dexterity

Nordic public sector issuers skilfully managed through the market turbulence of the past year, capitalising on their credit strength and funding flexibility to seize the often rare windows of opportunity to execute issuance across public and private markets in good size and different structures. To discuss their experience, DZ BANK and GlobalCapital brought together some leading Nordic public sector issuers and investors to analyse the key trends and developments that shaped the market across the year, and what they expect to see as we move into 2023.

Left to right: Petersen; Kontio; Brusas; Kemmish

Participants in the roundtable were:

Antti Kontio, head of funding and sustainability, Municipality Finance, Finland

Angela Brusas, director of funding and investor relations, Nordic Investment Bank, Finland

Daniel Aagaard Pedersen, head of funding and investor relations, KommuneKredit, Denmark

Jenny Lale Petersen, SSA origination, DZ BANK

Richard Kemmish, moderator and GlobalCapital contributing editor

GlobalCapital: The biggest story of the year has been the Russian invasion of Ukraine. How has that changed your organisation's activities and what has been the impact on your funding need?

Brusas: First of all, obviously NIB condemns the war. It has been a shock to all of us and that is where our main thoughts have been.

NIB's direct exposure to Russia and Belarus is very limited, less than €10m. We haven't signed any new loans to Russia since 2014 and to Belarus not since 2012. So far, the indirect impact of the war also seems to be limited.

What we have seen is a flight to quality. Normally when there is turbulence in the world, people tend to turn to high quality names. So, also, this time around. This has actually been a record year for us. There has been a big demand for lending, which has meant our funding programme has grown substantially. We came to the market pretty soon after the war broke out with both a green bond in euros and also a dollar benchmark. Both transactions were oversubscribed and we were able to upsize the dollar benchmark — so, we can see investor confidence was there.

So, at the end of the year now, we can actually say it has been business as normal — or even a better year. Although it has been horrible with all of the news, the impact on our business has not been bad.

Kontio: The war itself has not had a direct impact on our clients. Our clients still need to do long-term investment and that need hasn't disappeared. I guess the only place where it has had an impact is on the lending side with the energy companies. Normally we are outside the energy company financing because it is a competitive market, but now there is approval for us to finance the municipal energy companies, we get the 100% guarantee from the municipality and we can finance the collateral. This is a big thing; we haven't seen much lending coming from that source yet but this could change, of course, depending on the hedging costs.

Where there has been an indirect impact is on inflation. So, for example, the cost of construction is going up. We don't really know how much impact that will have on social housing production.

Putting this all together, it's very small changes. But on the funding side, like NIB I would say we have been flexible. We have changed our plans many times this year and we have been very successful, even though funding volumes have been quite stable. When the year started, we planned to issue between €9bn and €10bn and most likely that's where we will end up.

We have been more active on the tactical side — for example, Norwegian kroner, sterling, these kind of markets — and we have done fewer strategic benchmarks this year, so that has been the biggest change in our funding.

Antti Kontio, head of funding and sustainability, Municipality Finance, Finland

Pedersen: The first tier elements – the direct balance sheet impact – I would say have been negligible to Kommunekredit and Denmark. Overall, the Danish municipalities have not set forth any immediately relatable initiatives to the war in Ukraine — at least, not that directly hit KK's balance sheet. There are some elements of helping the NGOs in the area but nothing that hits us directly.

But the second tier projects and movements have begun. District heating is a major part of Kommunekredit's lending portfolio. As a result of the energy crisis, district heating has really taken the political centre stage — not just for politicians but for the general public as well. This has accelerated the already ambitious plans to increase district heating in Denmark with our members and municipalities, to reduce the dependence on gas.

GlobalCapital: On the energy point, you all benefit from very solid ratings. To what extent is your potential exposure to energy problems a credit issue?

Brusas: The minor impact on spreads is mostly because of general market volatility. As a result of the energy crises, there is an increased need for energy security and independence. But this is also the moment to accelerate the green transition. For a bank with an environmental mandate, financing renewable energy sources and companies in transition comes naturally. That is a long-term strategy of ours.

Petersen: We were roadshowing with Nordic issuers and they were expecting questions on the war and on the situation regarding the border with Russia. But the questions investors had were only related to energy. How is the energy situation? How is the supply going? Any shortfalls to be expected in winter? This is the main worry that everybody has, as Daniel said, for the upcoming cool season.

GlobalCapital: In general, with the volatility around the war, how has it affected the spreads of your bonds?

Kontio: I am actually surprised that there has been very minimal impact on spreads. When we look at government bonds, they have been pretty volatile as a result of some technicalities but agencies have been quite illiquid. Our euro curve has been pretty stable. But now, as we go into next year, volatility is going to be there. In euros I guess the swap spread may be going down, so most likely there will be some impact on the credit spreads as well.

GlobalCapital: Govvie spreads or swap spreads? Which changes have more impact on your bonds?

Pedersen: We always take everything back against asset swaps, so I completely agree with the points already raised. On an asset swap level, I won't say it's unchanged but it's not far off, either.

The big metric here is the govvie spread but, as has also been raised, it's a function of what the swap spreads have been doing. The technical needs in the repo market and for collateral are not something that we have seen in the asset swap pricing in our bonds. We have obviously widened some, but I think there is a fantastic amount of insulation in the SSA market.

There has been little to no influence from our proximity to Russia on our asset swap spreads. The movement is a consequence of the market pulling us slightly wider, rather than any proximity to Russia and Ukraine, in my opinion.

GlobalCapital: You raise lots of points that I would like to come on to. Jenny, can I ask you more generally about the SSA market and how it compares with other markets, bearing in mind all these factors that we have been discussing. Compared with covered bonds, FIG or corporates, for example?

Petersen: I agree with what has been said already about the flight to safe havens. That has helped the market. But it also helps that that this funding is reliable, that funding sizes have been pretty much unchanged and that investor work has been undertaken — including virtually in recent years. That has helped a lot to give investors confidence.

Daniel Aagaard Pedersen, head of funding and investor relations, KommuneKredit, Denmark

The most interesting shift that we have seen this year was the extremely strong request for private placements. Structured is something that has come back significantly, especially because of the change in rates. Investor targets that have been very far off are now being fulfilled pretty easily.

Covered bonds have had a record year. So, I would say, comparing sizes in different markets, it's a difficult question to answer. It is more about what investors really want and rely on and it is also about what is going to come along next year. Are covered bonds going to have another record year or are SSAs taking over again?

GlobalCapital: If you compare covered bonds and SSA bonds, which is the more able to cope with the volatility? Which has the better deal execution? Has covered bond supply been an issue for SSAs?

Petersen: I would have answered that question differently a couple of months ago. Now I would say it is difficult for both. It just has to be about the right window. If a bond does not work, it is not so much about the spread — it is more about the investors not wanting that name.

GlobalCapital: We hear the word 'window' a lot more nowadays. What has been your approach as issuers towards timing of deals and flexibility?

Brusas: It is always crucial to find the right windows. But being a smaller issuer is actually a benefit in times of turbulence, since we don't have to be in the market all the time. This year, for sure, the windows have been fewer and shorter and they required issuers to take fast decisions. Also, diversification is really important. We have done it through the years to be visible in different markets — in Australia, in sterling, in New Zealand and, of course, in the Nordics — in case there is one market that doesn't work for a while. This year we have been able to adjust to circumstances and carry out our usual funding strategy.

GlobalCapital: Presumably when windows are narrow, and there is a lot of volatility, it is easier for the big issuers to dominate those windows. How do you navigate around them?

Kontio: I can only agree with Angela that you need to have the tools in place, as many tools as possible. A good example happened this spring, when the market was closed but the private placement market was booming. We issued roughly €1bn in private placements during that time. So, there was no kind of deal execution risk. We just found a new way to do things.

But then, of course, it is not ideal from the continuity perspective when you want to be active in the longer benchmarks in euros. As I mentioned, we have been a bit too reliant on the tactical markets this year, but this takes away the pressure that you need to print on a certain day.

GlobalCapital: Daniel, are you also using the tactical markets such as MTNs?

Pedersen: We definitely have the same idea about reducing risks by using PPs or taps. KommuneKredit has a concentration rule: we cannot exceed €1bn in any one ISIN, so use of our PPs and taps, in particular, can be slightly more difficult for us.

With regard to the reduction of risks, I am reminded by a podcast I listened to recently about aviation. When flying a commercial airline and on approach for landing, the pilots will continuously ask themselves, "is there any reason I shouldn't land?" They are scanning their equipment, position and using their experience to look for a reason, a risk — and if one thing falls outside the scope of what they have agreed upon before going in they will do a go-around. That's very much what we did as issuers a year or 18 months ago. We were looking at a window and saying, "is there a larger player occupying the window? Is there a too familiar credit that we going up against? Too much congestion? Something that feels awkward?"

I think that has changed. We are now actively looking at "can we land?" rather than "is there a reason for a go-around?" We do that because there is a difference between the aviation model and the issuance model now. The assumption in the aviation model is that the landscape will be the same if you do a go-around — that is, you will get the same opportunity, the same 'market'. This assumption held in funding too, a year ago, but I think we can all see windows opening and — especially — closing much quicker nowadays.

Kontio: I like Daniel's phrase. Each issuer is a plane, and only one plane can use the runway at a time usually. We may also run out of fuel. The problem we have is we don't have the air traffic control tower. No one is telling you that it is safe to land.

Petersen: It is, sadly, a fact that windows are narrower. The runway has got shorter, so you need to push the aeroplane down. It also means you sometimes don't get exactly what you would like, but you get a deal printed. If you have the flexibility — a full fuel tank — then you have a backup. The problem is at a certain point in time you need to be in the market, so you do not have four months of flexibility but rather you have one month — but in the one month there could be two good windows. Flexibility is key – you have to be prepared and have everything ready.

What was a 'go/no go call' was 99% of the time a 'go call'. Until recently, there was not so big a possibility of it being a 'no go call'. Younger colleagues have perhaps never seen anything but a very stable SSA market, where all transactions have worked. We are going back to a shakier environment and you come back to the question of how you will tell investors that sometimes it's a 'no go call', nothing will happen. It's not the case with Nordic issuers this year.

GlobalCapital: The passengers expect to land. Investors in SSAs traditionally want a lot of predictability about when the plane is going to land. But they also want a lot of liquidity in the bonds. How do you avoid the stigma of pulling a deal? Have you had difficult conversations with investors?

Brusas: No, not really. We have been lucky enough to carry out the normal funding strategy this year. So, the timing has been good when we have decided to come to market with benchmarks. The execution window is smaller and risker, but we have managed to pick good execution windows, and haven't had to pull anything.

When you run out of fuel, you can put on the electricity instead. It has been really good that we have the MTN market that has been functioning really well this year. We also usually do 60 to 70 private placements a year. Obviously, because of interest rates, this year we are going to end up doing 100, roughly. So that market has again worked very well.

Kontio: I think it is important to have an established profile. When you have a liquid curve you are committed to issue, so then investors will understand that you are going to come back. Of course, if you do only one benchmark per year and then you change your plans, it is going to be very difficult to explain that to investors.

GlobalCapital: With this market volatility, with short windows and with the bund/swap spread rates being volatile, how do you set a starting point for price when you are trying to launch a deal? is it just a large new issue premium?

Petersen: For the Nordic issuers, the new issue premiums we have seen were not that different from recent years. When a deal hasn't worked, it hasn't just been about the price. It has been about investors not really wanting that name at that time. I doubt if you can sell it if you just add 5bp, 8bp or 10bp of new issue premium.

Jenny Lale Petersen, SSA origination, DZ BANK

The problem is rather at the long end — do the investors like that or not? — but you have the option to go shorter. And when the curve is flat, how much do you put on the end? Or do you take the safer option and just go shorter?

GlobalCapital: Issuers, I'm sure you pay what you have to pay in terms of new issue premium to get a successful deal. But at what stage do you say this is actually starting to reprice my secondary curve?

Brusas: It is always tricky to get the price right. It's not just secondary market performance you need to look at; you have to look at other issuers' recent issuance and then have the conversations. You need to get it right — the investors have the choice of staying away. But, again, it is important that you have the fundamentals in place and access to different markets. If it is getting really expensive doing dollars, you can turn around and do euros or other currencies. Or do other maturities. We are not doing very long funding anyway, but if you are you can then choose to go shorter, for example. You need to have the toolbox, to have other options.

GlobalCapital: Daniel, do you have any concerns about repricing your existing curve by paying too much of a new issue premium?

Pedersen: Constantly. That's our job, right?

But I don't think in the current market we should be very bullish. We have a long tradition in the KommuneKredit funding team — I would almost call it a mantra: today's transaction is the first marketing tool for the next transaction. With us being relatively small, compared with the EUs and KfWs out there, what is really important is that when we do something we get a deal that works. We cannot turn around next week and make up for lost ground by doing a new benchmark with a slightly larger new issue premium and make everyone happy again.

Angela has been touching on many of the same elements that we have been thinking about. If we can, as much as the balance sheet allows us to, we choose a tenor that we know works for investors, we choose the product — whether that's dollars or euros or a tactical currency, and we choose something that has some ground to it from our side *and* from the investors' side.

Other than that, the sobering reality is that we are relatively small vessels in a giant vortex in the sea. We cannot change gravity or the market. So, regardless of what we might think, our perception of secondary and everything, at the end of the day we need money and we need investors to lend that to us. I diligently try to make sure that I do that at the lowest cost, but there will be costs — especially now — and I'm very worried about coming out with something that's needlessly tight just because I think that's the right price.

Kontio: I fully agree with the recent comments. On pricing, I am pretty confident that the banks that we usually have on our trades know where our curve is. They know the market. I am not so worried about the pricing.

I am more worried about timing, if there is good karma on a particular day. If you choose a bad day, you will end up with a disaster. That is what we have seen this year. It may be one or two investors who don't participate for some reason — it's normally not the pricing — and that can build up to a very different outcome. And that's very difficult to fix.

GlobalCapital**: In investor relations, everything changed completely because of Covid. How is your approach to investor dialogue and roadshows changing?**

Brusas: We are back travelling now. We found it a little bit challenging during the pandemic. Of course, we organised virtual meetings but you can't say that it's the same thing. It depends which investors you are talking to, it depends on the jurisdiction. It's a different approach. During the pandemic portfolio managers have changed and issuers have changed, so it is important to get out again, to meet up and to get on the same page.

I still think its super important to meet up in person. In Asia you can have lots of long meetings, but then it's the walk to the elevator when one big important thing comes up and that makes the difference — and you can't get that over Teams. Naturally, we need to find a balance between actual travelling and virtual meetings.

Kontio: We have the same approach. Yes, we have some virtual meetings but they are not that fruitful. We all understand that, especially now there is a smaller investor base.

We are also trying to take advantage of virtual meetings, though. I am not saying that everything has to be virtual, but we can do more because we don't need to be travelling all the time. If there is only one meeting somewhere, maybe it is best to do that virtually and concentrate on areas where you can meet more investors. But we are back, so that's good.

Pedersen: It has changed less than I feared it would have a year ago. I feel we are much closer to something that makes sense and something that's sustainable. We are travelling less, but we are travelling. And we – as an industry – have rekindled the love of meeting people again and I feel that it's mutually beneficial. Investors are more or less voicing the same fatigue with virtual.

Having said that, the entire industry has historically been deprived of a lot of working days simply because of travel. When looking at our carbon footprint, travel has also been a huge contributor. It makes a lot of sense to integrate virtual meetings, but I will be a fierce advocate that virtual can only be a supplement, it cannot be the backbone of building relationships. I do believe that investors buy into the width of the bond, not just the one bond in particular on its pricing date. That's what we are doing at an investor relations meeting. We are showing them our mentality, what our strategy is, what they are buying into with this bond and the next one, and hopefully the one after that. It is more difficult to do that solely virtually.

GlobalCapital**: Jenny, when the issuers aren't there and you are speaking to investors, do they actually want these meetings?**

Petersen: Yes. It's a clear yes. It's a people business. We have been roadshowing with MunFin recently, it makes a big difference. But it's better to have a virtual meeting than no meeting at all.

With requests for virtual meetings you are often getting the answer no. The fatigue is definitely there. With physical meetings it is sometimes yes, sometimes no. It depends. When are the work from home days? Sometimes, when people really want to see that issuer they will come into the office.

On the other hand, virtual meetings were very exciting at the beginning. It was very good to see each other. But in the second year of the pandemic, with half the people working from home — probably not properly dressed with a tie, and the camera off — then you just mentioned the most important details of the presentation, what has changed and some things you want to highlight. Virtual is good for that. But to hear the feedback, having investors share their concerns, that was clearly missing. To me it felt more and more like a one-way street.

GlobalCapital: Angela, you have issued in Australian and New Zealand dollars - not an obvious choice for a Nordic investment bank. What are the lessons from that?

Brusas: I can only emphasise again that diversification is important. It has been great to be active in sterling and in the Australian and New Zealand dollar markets, in addition to the US dollar and the euro. We need to swap into euros, since I don't have a real need for sterling, Australian or New Zealand dollars, and that doesn't always work. This year the New Zealand dollar hasn't worked for us. But, for example, in the Australian dollar we have done a fair amount. We always compare the cost for funding in these currencies versus our US dollar benchmark curve.

Angela Brusas, director of funding and investor relations, Nordic Investment Bank, Finland

GlobalCapital: But it's not a free option. Presumably it's more difficult from a documentation and disclosure point of view?

Brusas: Not really. We have the programmes for the Aussie and New Zealand dollar. It is very straightforward. And we have been doing this for years, so the lawyers are very familiar with the documentation.

Pedersen: We are all looking at more or less the same markets. KommuneKredit isn't looking a lot at Kiwi but it is looking at Aussie. We haven't had a chance to go there for funding for a while but, as Angela was saying, it's very much a basis swap inefficiency.

We are trying to employ a strategy where the tactical currency that we have done more recently has a lower threshold to meet in terms of cost of funds. For us, that has been sterling — especially in 2021, when there was a lot of issuance. We have really made good progress with that.

Our tactical currencies, we aren't afraid to admit, are very much driven by our cost of funds. We try to see if we can do more in fewer markets in selective periods of time. Sterling has been the market and currency that has been working recently, and therefore it probably has a lower threshold in terms of cost of funds versus, let's say, a Canadian dollar or an Australian dollar — which, if it's the first funding activity for a few years, probably has to beat something (such as sterling) by more than a few basis points for us to take a new leap of faith.

Having said that, diversification is important, especially in the year that's coming up. It is actually one of the most fun bits of funding. There is really some strategising going into this. It might be only a single basis point or two that makes the difference — and, to be honest, when you have a balance sheet of €40bn-€42bn, it doesn't change the needle much if you are taking out 1bp on A$250m. But taking that leap of faith into a market can definitely change your funding perspective. It's a thing that we spend a great deal of time strategising on.

Kontio: It's the same story for Munifin on tactical markets. In addition to all of these comments, the reason tactical is good is that you can smooth your redemption profile— so, if you do only €2bn benchmarks then you are going to have big peaks that may be difficult from the refinancing perspective. So, we try to smoothen the redemption profile.

We always compare pricing to our euro benchmark curve. Whenever we do Nokkie or sterling, it needs to do better compared with euros — and if it's not, then what we say is it doesn't make sense to us.

But, yes, it's a lot of fun. Especially this year, the euro callable product has been there. We have done €2bn of euro callables because of the volatility going up — so, with these call options, it makes the coupon quite attractive. So, it has been a nice way to do something new.

GlobalCapital: Is the increase in MTNs entirely because of the volatility?

Petersen: I would say it's because of the volatility, but mostly because it's a different market to target. And there is the chicken and egg thing: the investors asked for structured products and the issuers were happy to fill that gap instead of going for benchmarks. It's not that volatility is currently the driver, it's more the rates.

GlobalCapital: And the shape of the yield curve, the flattening?

Brusas: In general we have seen shorter maturities this year. It has been a game changer having access to different markets, including the MTN market. We have seen many more private placements going through than previously. We don't do a lot of structures but the callable product is one that has really worked well. Plus a little bit of CMS spread product as well.

GlobalCapital: Antti, you mentioned Nokkie. I would like to ask generally about funding in the Norwegian, Swedish and Danish markets. With all of the things we have been talking about, is it the same in the three markets — or are they buffered from the external shocks?

Brusas: Nordics we need on the lending side, so we don't have to do cross-currency swaps. So, whenever we are able to take in Norwegian, Swedish or Danish currency we are happy to do so. But again, with the pricing we also compare everything with dollars or euros — so it has to make sense. It is not like we need it on the lending side, that we have to come to the market. It also has to work price-wise.

And then, if we think about the Nordics this year, what is common for all of them is that we have been able to issue green bonds denominated in these currencies. We issued the inaugural green bond in Danish kroner early this year. As we have seen in all markets, the sustainable label makes a difference these days. It doesn't matter which currency you are talking about.

GlobalCapital: Daniel, are you finding that Scandinavian market trends mirror euro trends, or is it different in its behaviour?

Pedersen: We spend a good deal of time looking at Danish kroner. It's somewhere in between a tactical and a strategic currency for us. It is strategic, so we want to be there and it makes so much sense, but it's a market that we cannot rely on, as we can euros and dollars, simply because the market movements have ben asymmetric to what has been happening in euros. Danish kroner, at the start of this, were very volatile. It felt as though we had the worst performing currency and assets before we politely passed that to the UK!

On this backdrop, Danish kroner have not been hugely productive for us this year, especially because the covered bond market in Denmark has been very difficult. Early in the fourth quarter of last year, a 30 year Danish covered bond had about a 1% or 1.5% yield – and we have topped out at close to 6% this year.

We continually talk to banks about what's possible. But sometimes there are forces here that are stronger than what you are able to combat, and obviously there has been a big outflow from Danish kroner investment pools. Danish kroner, Norwegian kroner and Swedish kronor are close to our heart. We have a very good reach with investors and will continue to develop that further. What is unique about these markets is that they work for us at the long end and at and the short end. Our balance sheet needs funding very long from time to time, so it's very important for us.

Kontio: This has been a very busy year in Nokkie. We have done almost 20% here. I don't have one reason for why that is, but we have been constantly active in this market — so we do have an established investor base. For some reason, they seem to like the Finnish issuer – possibly also because we are zero percent risk weighted. We are happy to be here and it's the Nordic family — so we want to be as present here as possible. Unlike NIB, we don't have lending in these currencies so it is purely based on pricing.

GlobalCapital: Historically, Nordic rates issuers have been very popular with Japanese investors. Is that still the case? Are you seeing enquiries from Japanese investors on MTNs or even benchmarks?

Kontio: Over the past few years, this market has been getting smaller. As in Europe, there has been more discussion on the retail side about what people understand and what they can buy, and there is more regulation around that. That is happening in Japan and it means that some of the houses have stopped providing these opportunities for retail. Time will show whether the structured note Uridashi market will return or not.

Brusas: We haven't been that active in Uridashi for the past few years. It is a very small part of our funding. What we are also missing is the Japanese investors in the long end of the Australian dollar market. We used to see more of the 10 year or longer issuance going into Japan and that has been lagging. Some of the Japanese investors take part in benchmarks, but in general we would hope to see more interest out of Japan.

GlobalCapital: You have all done green or social bonds relatively recently. Is that a market that is still growing as fast as before? What is the outlook?

Brusas: We do see a continued interest for it. Of course, there are a lot of developments in the market but we do see demand for the normal use-of-proceeds green bond. This has been a record year for us — we are at €1.1bn equivalent. Whatever currency you choose, the first question is: can you do green? We are still in the situation that we don't have enough eligible assets. Demand is bigger than supply.

But there is a changing focus. Investors are not only looking at the green bond — and what projects you are going to finance — but also at me as an issuer, so you need to have your governance issues and your environmental and social risk assessment in place.

GlobalCapital: Does that potentially invalidate the whole use-of-proceeds model? What matters is the whole organisation, not the use of these particular funds?

Brusas: That's a good question. We still see demand for use of proceeds bonds because there are dedicated green funds, for example. But we are being innovative; there are new products coming up. We started a year ago to give out sustainability-linked loans on the lending side, trying to move the hard-to-abate-sector companies into a more sustainable future. This is something that investors are also interested in but there is no good product for it right now. We don't like the sustainability-linked bond, being a bank. But, as mentioned before, there is also more focus on how sustainable the issuer is, in addition to the labelled bonds.

Kontio: The smallest execution risk you have is euro green. For many issuers who now have green programmes in place, maybe 5%-10% of the lending is green and 90%-95% something else. So, then, how can you have an impact on the other side of the business as well? That's where the holistic approach comes into play — but it's not good either if you wrap everything as sustainable. Everything we do is sustainable and that's it, no impact reports. Investors really want to see impact metrics. How is this going to improve the situation?

I fully agree that the green bond market is there. It's going to be there at least for the time being —but it would be nice if there could be a clear way to look for investors, not just green side but everything. We have ESG ratings now in place. Is that the way forward? Are the ESG risks the way to look at it? What is going to be the main way to look at this holistically? I don't know.

GlobalCapital: **Daniel, do you buy the line that everything you do is in line with sustainability goals?**

Pedersen: Absolutely, I would definitely buy that! But I would also say that I think it's the right move. I have had a little bit of an issue with green bonds in the SSA market versus corporates, for instance. Our role in society is holistic, for all of us. We are servicing something that's much bigger than ourselves. KommuneKredit is proud to drive the transition to green in Denmark. I completely understand the current 'use of proceeds' with a carve-out of the balance sheet — but, to be honest, I think we need to be rated on our entirety.

A green bond and a carve-out of the balance sheet makes sense for a shipping company that has an actual vessel they can buy, if they get proceeds at a better financing cost. They then buy a vessel that's more green. That makes sense, and that's direct: here is funding, here is something that is better for the environment. If we are being completely honest, that's not necessarily the same impact that we have, because our general funding purposes are much more holistic. I completely agree that currently using the carve-out method is right. That's why we have updated to a new Green Bond Framework that is partially aligned with the EU taxonomy, and we have ratings from Cicero. I just hope that in the future we are transitioning much more to the holistic. It should not be the cherry-picking of assets; it should be our entire governance, our entire being in my mind that will drive the transition further and faster.

Petersen: What has just been said covers all the layers that this topic has. The first layer is the euro green market for SSA issuers. It is the easiest to pick. Daniel is right, we need to service society. And I agree with what Antti has said about what the market is doing here. Having this holistic approach is an easy one. You can just tick the box.

But the deeper you go into this discussion — and we see it with the green taxonomy — is it just nice to play with the clean kids? The ones that are green already? Or do we want to have a say with the muddy kids? The dirty ones? Not just greenwash them, but take a holistic approach? If a company that has nuclear energy issues one green bond, what does that mean? Is it something that goes in the right direction.

I really liked the development just 10 years back. Now, it is so established. Then, at a certain point, the impact reporting also picked up. This is really something that investors are waiting for.

The green bond market is so well established — there is no question at all. But what about the social bond market? What about weapons delivery? And providers? Is there something social? Everyone would have answered that question a year ago with a clear no; now, we have this question of how to incorporate them. It's interesting where this is going.

Speaking of DZ BANK and Nordic issuers, it is very easy to serve our co-operative network base because they do have this holistic approach. They always looked at the issuer itself — but it makes it difficult sometimes for them to invest with that approach because it excludes a lot of other, non-Nordic green bonds, and there I question whether we are yet there with that approach.

GlobalCapital: **Will there be a social taxonomy ever, or will it be a market-defined sector rather than an EU definition?**

Brusas: Discussing the usability, just a couple of weeks ago there were efforts to give guidance on how to use the taxonomy and the EU green bond standard — because right now there are big challenges with the usability, so hopefully they will take on board all of the advice that the market, those with hands on, are giving them. I think they are picking up something. Maybe at some point we will arrive at something that is actually usable.

Kontio: Munifin has been active in social bonds for the past two years and I see that the topic is difficult. What is social in a Nordic context compared with developing countries?

The ICMA principles are very clear: you have the target population and that's how you build your framework. But if you have a taxonomy, it becomes very, very difficult. You come up with all of these pan-European problems: what is social in Spain might not be the same in Finland. So, I agree, it would be difficult.

Petersen: I fully agree. We need something that is handy and applies both to the green taxonomy, which is partially adapted, and the social taxonomy. We need to have a tool that we can work with, not just something that covers every little piece of what is upcoming all over Europe.

Pedersen: I very much agree. It's a classic case of what can happen when regulation is introduced to the industry. There are a lot of non-too-distant memories on this for MiFID and other regulatory implementations. There was a clear need for regulation, post-financial crisis, but the first generation of rules and regulations employed made it almost impossible to actually do what you wanted to do. It hindered a lot of stuff. We are seeing the same in the EU taxonomy. It's so nitty-gritty that it makes it difficult to achieve what we want to achieve. Hopefully, a feedback model — where the market participants can give inputs on what we are actually looking for — can be quicker than it was with regulation after the financial crisis. I worked in a bank at that time and it was not a fun period to actually do deals, because the amount of documentation you had to do was big.

The holistic approach makes a lot of sense. I will, of course, admit that it is a little bit of a fairy tale to believe that the holistic simple model will prevail throughout the economy and across all assets because it is a lot more nitty-gritty, for instance, for corporates.

Brusas: On the EU taxonomy, we all find it frustrating and difficult and all that, but we also decided that we are going to try to align ourselves with it and we started out with the green fund pool. So, we did the first attempt last year and we are going to continue doing it. It is just a start. Being transparent is the key.

The drivers here have really been the investors because they were calling us up and asking, have you done the alignment? Will you do it? Can we have a discussion around it? And it was a really good discussion with dark green investors, because they already needed to disclose the alignment of their investments. More important than having everything fully aligned seems to be the attempt by issuers to do the exercise. So, for our *Impact* report we added an estimated alignment to the EU taxonomy. It goes with a disclaimer, but we are being super-transparent and giving arguments for the result. It is important to remember that when we started out with the green bonds as well, everything — including impact reporting — seemed very complicated as well. But we worked it out, so you just have to start somewhere, be super-transparent and then develop the reporting as we get more guidance.

Pedersen: That's a super-important point. What the EU taxonomy has done with flying colours is set some direction. It has given us something to debate. Let's hope that we can get it moving along the value chain — but it has definitely managed to set ESG at the forefront for the entire market.

Kontio: Now everything is voluntary. You can decide to become a green bond issuer, you can adapt the taxonomy into processes, or whatever. But you also have the regulation and the taxonomy is coming from that side. For us, because we are supervised by the ECB, there will be certain metrics that we have to report – for example, the green asset ratio, the amount of taxonomy aligned assets in your portfolio.

GlobalCapital: In one sentence or less, what will be the dominant theme for funding SSAs in 2023?

Brusas: Inflation, interest rates, recession.

Kontio: I had inflation too.

Pedersen: Central banks. There are recent examples of where central banks have had a surprising reaction function that led to a big move in markets. It's not easy being a central banker right now, and I fear 2023 is not going to be any easier.

Petersen: I was going to say that as well: central banks. The other thing is exogenous shocks. We need to manage the unmanageable in 2023. GC