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Amundi
Investment Solutions

Trust must be earned

Newsletter for Central Banks

Building together smart solutions to face a challenging environment

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For more on Amundi's thought leadership: visit our website

Dear Client,

Welcome to the fourth edition of Amundi's Newsletter for Central Banks, crafted by our experts for you.

In an environment of increasing macroeconomic and geopolitical complexities, our specialists share their views on global policy and investment themes important to Central Banks worldwide.

In this edition, we explore the complexities of the evolving geopolitical landscape, with a focus on the shifting relationship between China and the US and its implications for global markets. We also shed light on a common project with Fondo Latinoamericano de Reservas (FLAR), which resulted in the launch of an ETF tailored to meet central banks' sustainability goals. Finally, we examine the rise of green bonds in developed and emerging markets and the crucial role central banks play in advancing the green transition.

We hope this edition meets your expectations and invite you to share your thoughts with us!

Contact us at sovereign@amundi.com

What's new & coming up?

October 2024

PRI in Person Takeaways

Amundi participated in the 16th edition of PRI in Person, where our experts shared insights on sovereign engagement and sustainable regulation—read the key takeaways from this leading responsible investment conference.

Read more

October 2024

2024 US elections: macro, geopolitical, and investment perspectives

As the US elections approach, markets are increasingly focusing on the candidates' platforms and their implications for the economy and markets.

Read more

7 November 2024

WEBINAR
The countdown starts: US election results and market implications

Join our expert panel as they take a detailed look at the early election results, discuss next steps and their implications for investors.

Register to join

12 November 2024

WEBINAR
Amundi Investment Outlook 2025

As we look ahead to 2025, investors face critical questions about growth, inflation, and geopolitical shifts. Join us on Tuesday, November 12, for the launch of our 2025 Investment Outlook.

Register to join

Anna ROSENBERG
Head of Geopolitics,
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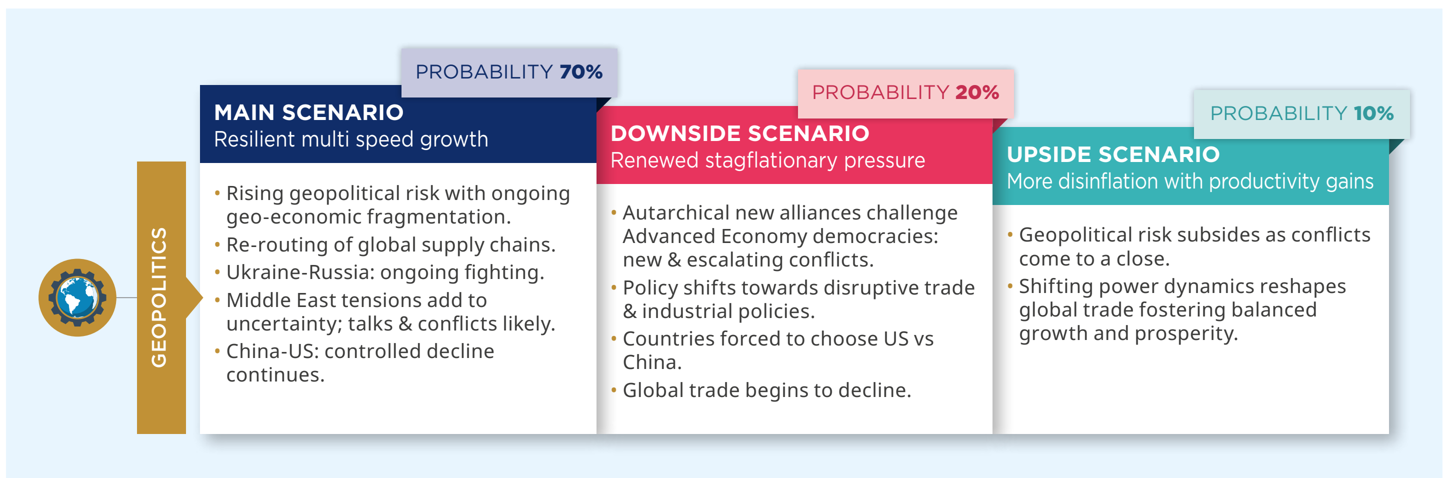
Growing Geopolitical Risks Require Investors to Adapt

Since Russia's invasion of Ukraine and the Hamas attack, we have seen worsening bilateral relations. More countries are contributing to higher geopolitical risk, which is evidenced by our Geopolitical Sentiment Tracker. It is likely that the level of geopolitical risk will grow further this decade.

First, there is the evolution of Russia's war goals: **it is increasingly likely that Russia's ambitions are morphing from territorial expansion towards eroding the Western-led global order.** In that regard, the growing Russia, Iran and North Korea ties are a game changer. For example, Russia's protection of North Korea at the UN Security Council, and its new military cooperation with North Korea, are allowing the latter to expand its nuclear capabilities without the ability of other countries to contain it. This is a tangible example of the growing risk caused by declining multilateralism and the more risky world we are moving to. **Protectionism, export controls, sanctions and tariffs will increase and cause more economic friction.** The United States-China relationship will deteriorate further, no matter who sits in the White House. **The situation in the Middle East also carries a significant risk of further escalation.** This overall dynamic will not change under Harris or Trump. As risks rise, investors and companies need solid frameworks to monitor risks, adjust and ensure they are positioned to benefit from the changes underway.

Main and alternative scenarios



Source: Amundi Investment Institute, October 2024.

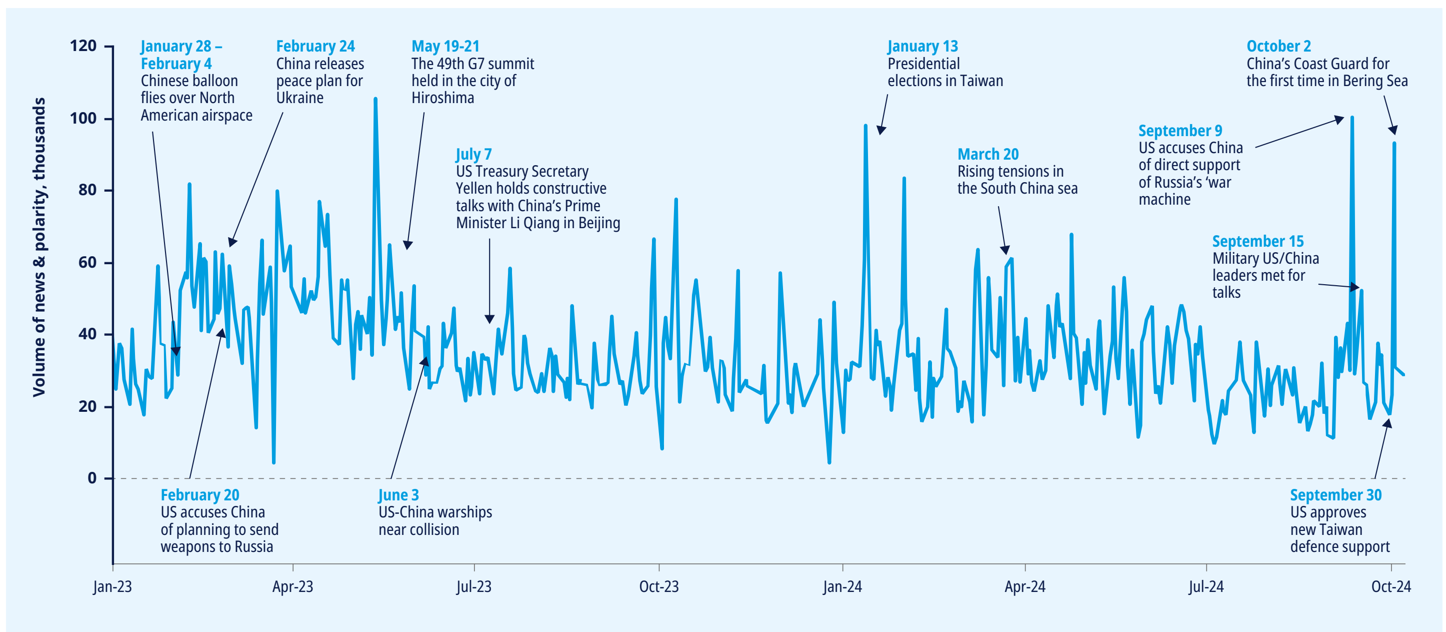
A focus on the United States-China relationship

The past few years have been difficult for US/China relations. Our Geopolitical Sentiment Tracker illustrates the rocky relationship and events which lead to a spike in risk in the bilateral relationship. **US/China ties can be classified as a Great Power competition, in which the US seeks to maintain its hold on power, while China seeks to expand it.**

The next US administration will preside over worsening China ties, no matter who sits in the White House, as the competition is likely to intensify. Under a second term for Donald Trump, the US-China relationship would likely be shaped by trade disputes with broad additional tariffs on Chinese imports to the US likely, although a blanket 60% tariff on all goods coming into the US is unlikely. However, specific sectors would likely be targeted with high tariffs.

In a similar way, a possible Harris administration would likely continue with Biden's strategy towards China, hitting some economic sectors, especially sensitive technology sectors, with more export controls.

US/China relations – Amundi Investment Institute Geopolitical Sentiment Tracker



Source: Amundi Investment Institute, Geopolitical Sentiment Tracker – bilateral relations. Data as of 7 October 2024.

Claire HUANG
Senior EM Macro Strategist,
Amundi Investment Institute

The People's Bank of China: Evolving Through Complexity

The People's Bank of China (PBoC) is adeptly navigating the intricate landscape of geopolitical pressures, striving to reduce reliance on a dollar-dominated financial system while implementing cross-cyclical policies that adhere to economic and financial logic. This balancing act is crucial as the PBoC fulfils its multifaceted mandates in a rapidly changing global order.

The Changing Sea

China's central bank has undergone significant transformations over the past five years. In 2019, it was restructured as part of a broader government institutional reform - the first such overhaul in a decade. Just under five years later, in 2023, the PBoC faced another restructuring alongside the establishment of the National Financial Regulatory Administration, which merged banking and insurance regulators.

These changes resulted in a reduction of the workforce at the central office and a decrease in management positions. The reporting structure also shifted, with the leading Central Financial Committee Work Group no longer residing within the PBoC.

Given these changes, one might question whether the PBoC's influence within China's policymaking circle has diminished. However, its mandates tell a different story. The PBoC has both legal and administrative responsibilities, with the 2019 and 2023 institutional reforms clarifying its 20 executive mandates. These include not only the design and implementation of monetary policy, credit, and macroprudential policies but also the regulation of market participants, and the promotion of the renminbi (RMB) internationally.

Beyond its daily responsibilities, the PBoC has also had to adapt to major shifts in the financial sector, driven by high-level political events. **The sector has awakened to a new reality, where political goals and mandates are now paramount.** A landmark moment was the Central Financial Work Conference in October 2023[1], where leadership expressed dissatisfaction with the intertwined issues plaguing the financial sector. Concerns were raised about potential financial risks, the low quality and efficiency of financial services to the real economy, recurring financial disorders, and inadequate supervision and governance.

The leadership emphasised that the financial sector must strengthen its political awareness, align with the country's fundamental interests, and enhance its sense of mission and responsibility. **The call to action was clear: the financial sector must address these challenges to contribute to building China into a strong nation and advancing national rejuvenation through high-quality financial development.**

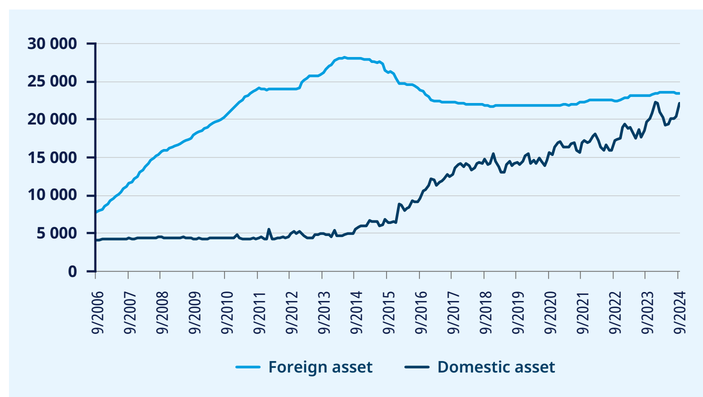
For Chinese leadership, the financial sector is the lifeblood of the economy and a crucial component of the country's core competitiveness. The PBoC, as a key player in this landscape, must strike a delicate balance between development and security in an ever-evolving world. **Its role in maintaining economic stability has taken on added importance in the content of heightened geopolitical risks and shifting global financial dynamics.**

Guarding Against Geopolitical Risks

Foreign reserves reached their highest point in 2014, following a period of rapid accumulation (Chart 1). While the total size of these reserves has stabilised, their composition likely shifted. In the wake of the Russia-Ukraine war, the State Administration of Foreign Exchange (SAFE[2]) has been vigilant, closely monitoring the effects of US sanctions.

1. 2 November 2023 Xinhua - Central financial work conference is held
2. SAFE is the national regulatory agency that oversees activities in China's foreign exchange market. It is overseen by the People's Bank of China.

Chart 1: PBoC Assets (RMB bn)



Source: PBoC, CEIC, Amundi Investment Institute as at end September 2024.

To effectively safeguard foreign assets, a robust defensive strategy must include:

- Reducing reliance on dollar-denominated assets.
- Developing an independent FX transaction and cross-border settlement platform.
- Promoting RMB-denominated contracts and settlements with trade partners.

Despite a rise in RMB trading, it accounted for only 3.5% of global FX market turnover in 2022, lagging far behind the USD's 44% and the EUR's 15%[3]. As of Q2 2024, the RMB represented just 2.1% of total allocated reserves globally, down from 2.8% in Q1 2022[4].

Transitioning away from a dollar-centric system requires a multifaceted approach, including building trust in the RMB among international trading partners and enhancing the liquidity of RMB-denominated assets. This process involves not only increasing the volume of trade conducted in RMB but also fostering a robust financial ecosystem that supports RMB transactions.

Needless to say, China still holds over $1.4 trillion in US Treasuries as of the end of 2023, with no clear alternatives for effective liquid reserve management. While the ambition to reduce reliance on the dollar is evident, the complexities involved mean that this transition will require time and the implementation of a clear strategy.

A Master of Adaptation

In response to the aforementioned challenges, the PBoC has embarked on an unconventional monetary policy trajectory. This approach diverges from the established frameworks such as quantitative easing (QE) and negative interest rate policies (NIRP), reflecting PBoC's innovative adaptations for its renewed mandates.

1. Structural Monetary Policy Instruments

The PBoC has introduced Structural Monetary Policy Instruments (SMPI) as a cornerstone of its monetary policy, in part to avoid blunt "bazooka-style" easing which is disliked by the top leadership. By mid-2024, the central bank had rolled out 18 SMPIs, with 10 currently operational and 8 phased out. These instruments are crafted to tackle specific challenges in the economy, **aiming to "support the real economy, promote structural adjustment, and enhance the effectiveness of monetary policy."**

Primarily functioning as relending tools, these instruments allow the PBoC to extend loans at below-market rates to banks, and non-bank financial institutions (NBFIs). **This targeted approach aims to stimulate investment in critical sectors or support financing in certain areas,** although the eventual take-up depends on the specific tool, and its effectiveness in the housing market has been limited.

2. Equity Market Support Pipeline

In September of this year, the PBoC initiated new programmes to support the capital market, marking a significant shift in its operational strategy. Two key tools have been launched to stabilise the market and enhance investor confidence. **The first is a swap facility for securities, funds, and insurance companies,** enabling these entities to exchange their holdings of fixed income and equity ETFs for high-quality, liquid assets like government bonds. Initially set at RMB 500 billion, this facility aims to improve liquidity for institutions facing challenges in asset liquidity.

The second tool involves central bank lending to support share buybacks, directing commercial banks to provide loans to listed companies and their major shareholders for purchasing shares. The PBoC will lend to banks at an interest rate of 1.75%, with an initial quota of RMB 300 billion.

PBoC has lent a total of RMB 743bn to NBFIs this year, representing 1.6% of its total asset. Once the first support tool is deployed, this line on PBoC's balance sheet will expand meaningfully.

3. Buying and Selling of Government Bonds

Moreover, the PBoC has begun actively buying and selling Chinese Government Bonds (CGBs). This initiative differs from the one-directional approaches of the Fed or the Bank of Japan. The PBoC's buying and selling of bonds could act as either tightening or easing forces. **This flexibility allows the Bank to respond to market conditions without a predetermined monetary policy inclination.**

Future developments will depend on the government's willingness to stimulate the economy and coordinate fiscal policy.

4. Monetary Policy Framework Transition with a New Policy Rate

In 2024, Governor Pan Gongsheng is advocating for a reform of the monetary policy framework, proposing the 7-day reverse repo rate[5] as the new policy rate. This choice allows for precise control over short-term interest rates through daily open market operations (OMOs), providing a nimble tool for liquidity management.

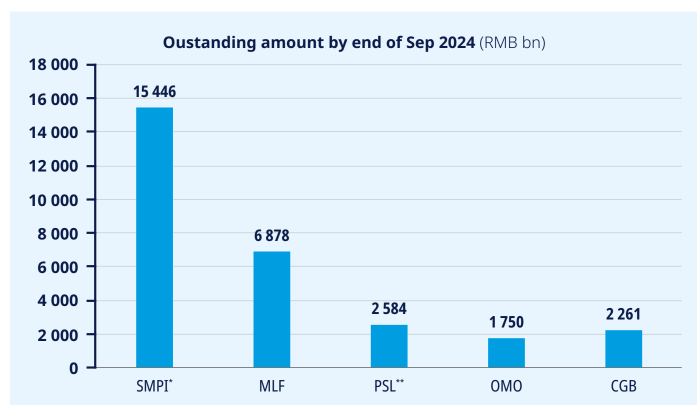
3. BIS Triennial Survey
4. IMF COFER
5. The rate at which the Central Bank borrows money from commercial banks within the country

Concurrently, the PBoC will phase out the one-year Medium-Term Lending Facility (MLF), currently exceeding RMB 6.8 trillion. To replenish reduced MLF liquidity, the PBoC is likely to increase net purchases of CGBs, lower the reserve requirement ratio (RRR), and ramp up regular OMOs.

In this broader context of monetary policy transition, a net increase in CGB purchases alone shouldn't be interpreted as a sign of monetary easing. A comprehensive view of changes in MLF, OMO, and CGB, alongside structural relending tools, will provide a clearer picture of overall interbank liquidity (Chart 2).

Thanks to the growing variety of policy tools, the PBoC's domestic assets are on the rise (Chart 1), and this trend is likely to continue, driving the overall expansion of the Bank's balance sheet. This will serve as a crucial indicator of any de-facto quantitative easing from the PBoC.

Chart 2: PBoC's liquidity management and structural relending tools



*SMPI size is by the end of Jun 2024. Source: PBoC, CEIC, Amundi Investment Institute.
**PSL: Pledged Supplementary Lending is a lending facility under which the PBoC directly provides loans to commercial banks with collateralization.*

The recent reforms and policy adaptations at the PBoC respond to China's dual domestic and international challenges. Domestically, restructuring efforts and the introduction of new policy instruments aim to stabilise the economy, manage financial risks and support key sectors. Internationally, the PBoC's efforts to reduce reliance on the dollar and promote the renminbi reflect China's response to rising geopolitical uncertainties and its desire for greater financial independence. These changes are crucial for strengthening China's economic security and competitiveness in a shifting global landscape.

Frédéric HOOGVELD
Head of Investment Specialists and Client Solutions, Amundi ETF, Indexing & Smart Beta

Empowering Central Banks with ETF Solutions to Meet Their Needs

In June 2024, following a months-long project led by its Board of Directors and Investment Committee, and involving close collaboration with central banks and other official institutions across Latin ,America, the Latin American Reserve Fund (FLAR) announced its role as a seeding partner of a Global Corporate Highest Rated ESG ETF launched by Amundi ETF, the Amundi Global Corporate SRI 1-5Y Highest Rated UCITS ETF[1].

This initiative aims to leverage FLAR's expertise in responsible investing to create an ETF that central banks and public institutions can utilise for responsible reserve management. This project concluded with a comprehensive RFP process, through which Amundi was selected as the ETF manager.

Introduction to FLAR

The Latin American Reserve Fund (FLAR) is a distinguished supranational organisation comprising nine central banks across Latin America. **Committed to enhancing financial and economic stability in the region, FLAR provides balance of payments and liquidity loans to its member countries.** Over the past 45 years, FLAR has established itself as a credible hub for connection and collaboration among central banks and official institutions, making it a natural partner for innovative investment solutions.

As a member of the Network for Greening the Financial System (NGFS), FLAR continuously seeks to align responsible investing principles with traditional reserves management guidelines – security, liquidity, and return objectives.

Like many central banks, FLAR and its members are required to invest in highly liquid, high-quality, and low-risk securities.

Issuing ESG ETFs

Two critical elements are essential for an ETF issuer to successfully manage ESG ETFs:

1. Capabilities and Experience in Designing Customised ESG Indices

ESG indices have become increasingly complex in recent years due to the expansion of available datasets and portfolio construction methodologies.

Amundi ETF, the largest European ETF issuer[2], has co-developed **ESG and Climate index solutions for public institutions since 2014,** when it co-created the first series of low-carbon equity indices for two public pension funds in Europe. Since then, our engineering and product teams have **significantly enhanced their capabilities to develop custom index solutions that incorporate the latest ESG and climate datasets and methodologies.**

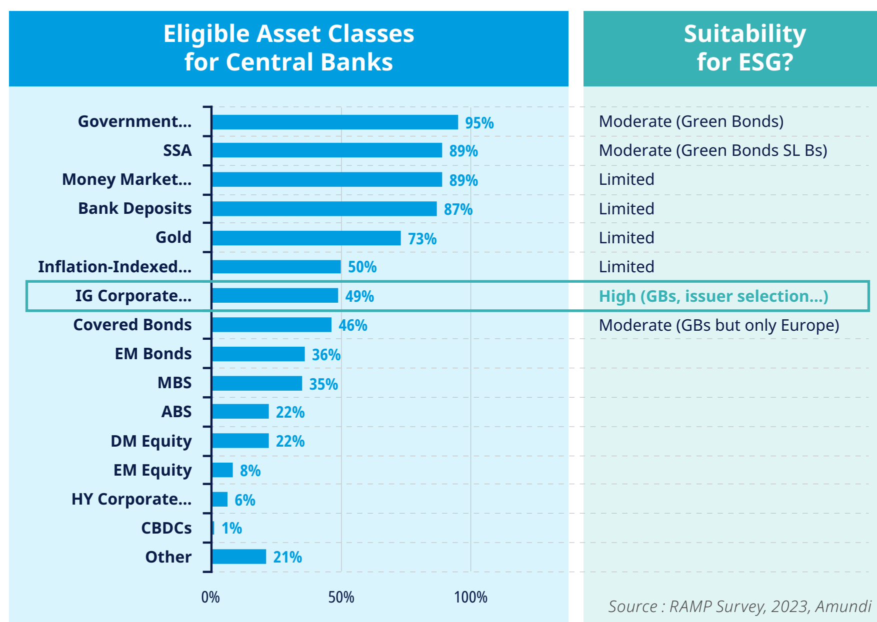
2. Active Ownership Policy Aligned with ESG ETF Objectives

While the construction of the ESG index – how securities are selected and weighted – is crucial for an ESG ETF to fulfil its purpose, the active ownership policy of the ETF issuer must also be carefully scrutinised to ensure consistency between the responsible investment goals and the effective stewardship of the assets.

Amundi's active ownership policy consistently ranks among the most assertive globally and positively contributes to achieving sustainable investing objectives[3].

1. Index Bloomberg Ticker: H38487US
2. Source: Based on ETFGI data as at end July 2023, Amundi ETF is the leading European headquartered ETF provider within the European market.
3. https://shareaction.org/reports/voting-matters-2023

Why a Global Corporate Short Term High-Quality ETF ?



Source : RAMP Survey, 2023, Amundi

The 2023 Reserve Advisory and Management Partnership (RAMP) survey conducted by the World Bank indicates that **high-quality investment-grade corporate bonds with short durations are highly eligible among central banks due to their low risk and high liquidity[4].** Furthermore, these bonds are well-suited for an ESG overlay, as ESG data is available for the vast majority of investment-grade corporate issuers.

The high-level index design principles were based on a cap-weighted approach with implementation of selected exclusions. This approach was chosen over a more complex, optimisation-based approach, to ensure a high level of transparency.

Key Characteristics of ESG Index

Criteria	Rule
Index Provider	Bloomberg with MSCI ESG data
Starting Universe	Global Corporate
Credit rating	AAA-A
Maturity filter	1 - 5 years
Hedging	USD Hedged
Seniority	Senior Unsecured (Unsubordinated) or Senior Secured.
EM/DM	Developed Markets only (as per Bloomberg Country of Risk definition)
ESG Ratings	- Securities must have an MSCI ESG Rating of **BBB or higher** - Unrated issuers from sectors with ratings are excluded.
ESG Controversies	Excludes any issuer with a **"Red" MSCI ESG Controversies Score** (equal to zero), which measures an issuer's involvement in major ESG controversies and how well they adhere to international norms and principles.
ESG Business Involvement screens	Adult Entertainment, Alcohol, Gambling, Tobacco, Weapons, Nuclear Power, Fossil Fuels, GMO
Minimum ESG exclusions	20% of parent universe

4. *https://openknowledge.worldbank.org/server/api/core/bitstreams/c0c2d54b-53e6-4af5-b2e3-5fcd8ba4e8f6/content*

Despite the high level of ESG stringency in **the proposed ESG approach, it is worth noting that the financial characteristics of the designed index align closely to that of the parent, non-ESG index,** as illustrated in the table below:

Financial Characteristics of ESG Index vs Parent Index

(as of 2024-07-31, in USD)	Bloomberg Global Corp A and above 1-5Y (USD hedged)	Bloomberg MSCI Global Corp A and above SRI 1-5Y (USD hedged)
Fixed Income metrics		
# constituents	2648	2181
Option Adjusted Duration	2.55	2.54
Yield to Worst	4.25	4.24
OAS	59.64	59.81
Spread Duration	2.59	2.59
Performances		
Perf YTD (%)	2.94	2.96
Perf 1Y (%)	6.91	6.95
Perf 3Y (ann., %)	0.97	0.99
Vol 1Y (Monthly, %)	2.88	2.88
1Y TE (%)	-	0.02
3Y TE (%)	-	0.04

For example, the ESG and non-ESG Global Corp A-AAA 1-5Y indices exhibit very similar duration, yield to worst, and option-adjusted spread, with a minimal tracking error of just 2 basis points over one year. This high level of similarity arises from the fact that the **performance of high-quality, short-duration bonds is primarily driven by common factors such as currency or sector, rather than idiosyncratic risks like ESG scores. This makes this ETF exposure particularly attractive. Furthermore, the ESG index demonstrates better performance in terms of ESG metrics, such as average ESG rating and carbon footprint indicators, when compared to the non-ESG index.**

Process and Timeline for Co-Designing ETFs

While each ETF co-design project has its own characteristics and objectives, the key milestones of such projects typically include:

1. Selection of Preferred ETF Issuer by Seed Investor

In this step, the seed investor selects the ETF issuer responsible for structuring the new ETF. This process focuses on **understanding the issuer's expertise in the asset class** from both portfolio management and index design perspectives, as well as other relevant considerations such as distribution capabilities and active ownership policy.

2. Construction of the Index Reflecting Seed Investor's Key Investment Guidelines

The index methodology construction requires discussions among the ETF issuer, index provider, and seed investor. The goal is **to identify and address the seed investor's investment guidelines and constraints,** ensuring they can be translated into an investable, transparent index. Some constraints may be contradictory (e.g., low tracking error vs. high ESG score), necessitating careful arbitration between options.

3. Structuring, Launch, and Listing of the ETF

Once the index methodology is finalised, the ETF launch process follows a standard procedure involving regulatory filing and approval, opening ETF accounts, seed investment, and ETF listing. Depending on the complexity of the initial requirements, **a typical co-designed ETF can take between 6 and 12 months to launch.**

The Amundi Global Corporate SRI 1-5Y Highest Rated UCITS ETF represents **a significant advancement in the responsible investing landscape for central banks.** By combining Amundi's extensive expertise with FLAR's strategic vision and the valuable insights and collaboration of other reserve managers, **this initiative effectively addresses the immediate needs of central banks to manage their reserves responsibly, and demonstrates that this trend is relevant not only in the developed world but also in emerging markets.** As central banks worldwide increasingly embrace ETFs as powerful tools for diversification and liquidity, Amundi remains committed to supporting their journey toward responsible investment solutions.

Read Amundi ETF's Interview with **Iker Zubizarreta Abando,** Chief Investment & Financial Officer at FLAR.

Read the interview

Alban DE FAŸ
Head of Fixed Income SRI processes and Credit Portfolio Manager

Sergei STRIGO
Co-Head of Emerging Markets Fixed Income

Green Bonds and Central Banks: Driving Economic Resilience through Sustainable Investments

In recent years, green bonds have emerged as a pivotal financial tool, bridging the gap between sustainability objectives and economic growth in both developed and emerging markets. As climate risks intensify, green bonds offer a unique opportunity to invest in projects that support environmental resilience while delivering financial returns.

In this interview, Alban de Faÿ, Head of Fixed Income SRI Processes and Credit Portfolio Manager, and Sergei Strigo, Co-Head of Emerging Markets Fixed Income, discuss the growing prominence of green bonds, the unique challenges they face, and the crucial role central banks play in integrating these instruments into their balance sheets and broader monetary policy frameworks.

Alban de Faÿ, Head of Fixed Income SRI Processes and Credit Portfolio Manager, answers our questions on integrating green bonds into fixed income strategies and their role in balancing financial and sustainable goals.

As green bonds gain traction globally, how have you adjusted your fixed income strategy to ensure green bonds contribute meaningfully to both financial performance and sustainability goals?

■ **Alban:** Green bond issuances follow financial principles that are rigorously identical to the equivalent standard bonds from the same issuer. Thanks to issuers disclosing the environmental benefits generated by the financed projects, investors are able to invest in dedicated impact strategies, pursuing financial returns while contributing to sustainable development.

Additionally, these strategies take into account the fair value of green bonds based on the credit quality of the issuer, rather than the transparency of the use of proceeds.

In 2024, the total outstanding amount of green bonds across all of Amundi's Alpha Fixed Income strategies reached €46 billion, with €7 billion specifically allocated to our dedicated green bond strategies. This significant allocation reflects the growing interest in sustainable finance and the critical role that green bonds play in funding projects aimed at combating climate change. It also illustrates that the largest portion of the green bonds market is held by regular investors, rather than by dedicated green bonds investors, which is a positive feature as it ensures fair pricing. Moreover, the *greenium*[1] is relatively low – ranging between 0 and -5 basis points – and is on a decreasing trend, demonstrating that investing in green bonds can be pursued without negatively impacting financial performance.

Finally, assessing the positive environmental benefits of green bonds requires additional effort compared to traditional bonds. As a result, enhanced analytical capabilities are necessary, which Amundi has progressively developed over the past years. In this context, we believe we are well-positioned to make investment choices that balance both financial performance and impact.

How do you balance the potentially lower liquidity and credit risks associated with green bonds against their longer-term ESG benefits?

■ **Alban:** The current green bond market shows no signs of lower liquidity compared to the equivalent standard bond market. While the strong demand in the green bond market may impact buying liquidity, there are no liquidity issues when selling. In fact, selling liquidity may even be easier due to high market demand for green bonds.

With regard to credit risk, we can conclude that it is identical between a standard bond and a green bond issued by the same issuer. Frequently, issuers come to the market in both formats.

However, the issuer's impact report allows us to estimate the sustainable benefits from the projects financed as soon as the first report is published, which makes us value the sustainable dimension of the instrument, regardless of the bond's maturity.

1. The greenium is the amount by which the yield on the green instrument is lower, compared with the conventional instrument.

Green bonds can play a crucial role in financing sustainable projects in a wide range of sectors, such as renewable energy, energy efficiency, and sustainable infrastructure, and thereby contribute to reaching the Paris Agreement objectives.

In recent periods of market volatility – due to inflation, rate hikes, or geopolitical risks – how have green bonds performed? Can central bank asset allocators rely on green bonds as a safe haven in turbulent times?

■ **Alban:** Green bond issuances behave similarly to standard issuances, with the primary difference being that green bond investors tend to take a longer-term position. If we observe different behaviours at the index level, these discrepancies are mainly due to sectoral or FX biases.

As a result, the green bond market is by no means a "safe haven". This can be seen by the fact that it is a market without covenants. The basic principle remains that we are financing a company, even if the process specifically identifies projects. Ultimately, the investor is exposed to the financial risk of the company and not to the risk of the financed projects.

How do you foresee the long-term risk-adjusted returns of green bonds evolving as the market continues to mature?

■ **Alban:** There is no reason to expect a different long-term risk-adjusted return compared to traditional bonds, unless a true green bond label recognised by investors is established, enabling them to secure a tax benefit or an equivalent advantage.

Before this can happen, **the prerequisite step is the establishment of the European Union Green Bonds Standard (EU GBS).** Only then could the EU provide, for example, a tax advantage for issuers whose green bonds follow the EU GBS or comply with recognised labels (Greenfin, etc.).

As central banks increasingly incorporate climate risk into their decision-making frameworks, how can green bonds help align monetary policy objectives with global climate goals? What role do you see them playing in the transition?

■ **Alban:** To help economies progressively align with global climate goals, central banks should encourage and provide incentives to companies to engage in sustainable business models. **As asset owners, central banks have a role to play by greening their own balance sheets, and green bonds are often instruments of choice for these institutions.** The International Capital Markets Association (ICMA)'s Green Bond Principles provide a robust framework that emphasises transparency, accountability, and environmental integrity in the issuance of green bonds. By adhering to these principles, issuers commit to using proceeds for projects that deliver positive environmental impacts, thereby supporting central banks' objectives of promoting sustainable economic growth and financial stability.

Moreover, the upcoming EU Green Bond Standard, set to be implemented by the end of 2024, aims to establish a clear regulatory framework for green bonds within the European Union. This standard will require issuers to provide standardised reporting and impact assessments, ensuring that the funds raised are genuinely contributing to the transition to a low-carbon economy. By enhancing the credibility and transparency of green bonds, **the EU Green Bond Standard will make these instruments more attractive to investors and central banks,** facilitating their integration into monetary policy frameworks.

As central banks are starting to consider climate-related risks in their asset purchase programmes, **green bonds can serve as a viable investment option that aligns with both monetary policy objectives and global climate goals,** effectively addressing two critical priorities at once.

Speaking with Sergei Strigo, Co-Head of Emerging Markets Fixed Income, we explore the role of green bonds in emerging markets, strategies for mitigating risks, and how liquidity and current volatility are managed in this growing asset class.

Emerging markets (EM) are often at the frontlines of climate risk, but also present significant growth opportunities. How are green bonds helping to bridge the gap between risk mitigation and return generation in these regions?

■ **Sergei:** Emerging markets are highly vulnerable to the impacts of climate change due to limited capacity and the lack of adaptation mechanisms to effectively address these challenges. Moreover, they face an unprecedented task of balancing decarbonisation objectives while maintaining a sustainable economic development path. **Policymakers, issuers, and investors – such as central banks – are mobilising rapidly around green bonds as part of the solution, as they are instruments that connect investments to projects with environmental benefits.**

Furthermore, green bond issuers are required to monitor and report the impact of the capital deployed. These characteristics, combined with the attractive yield potential found in EM, **support our belief that green bonds can serve as an effective financing mechanism in supporting the green transition in emerging markets.**

Emerging markets often have a different risk profile compared to developed markets—political, credit, and currency risk. How do you mitigate these risks and avoid greenwashing when investing in green bonds from issuers in emerging markets?

■ **Sergei:** Investing in green bonds from emerging markets presents distinct challenges, including political, credit, and currency risks, as well as the potential for greenwashing. **At Amundi, we have 25 years of experience managing EM debt, with a dedicated team of portfolio managers, credit research analysts, and a portfolio construction team.** We also benefit from the insights of specialised EM macroeconomic strategists and a geopolitics specialist from the Amundi Investment Institute, who provide invaluable macroeconomic research on key political risks in the countries where we invest. Additionally, our ESG analysis is reinforced by 49 dedicated ESG research, voting, and engagement analysts, ensuring a comprehensive approach to sustainable investing.

Our investment strategy is both active and research-driven, employing a dual approach that combines top-down and bottom-up analysis. On the one hand, we conduct in-depth macroeconomic research to guide our strategic portfolio direction, helping us determine which countries to invest in and which to avoid. On the other hand, our bottom-up research focuses on credit and ESG analysis, allowing us to uncover unique investment opportunities within the credit universe. We prioritise identifying issuers with improving fundamental drivers to ensure we invest in assets that deliver the best risk-adjusted returns throughout the investment cycle.

To address the issue of greenwashing, we have developed a proprietary Green, Social, and Sustainability (GSS) Bond Framework[2]. This framework follows a comprehensive four-step approach that combines issuer- and issuance-level analysis, along with continuous monitoring and engagement activities. It is implemented by our dedicated team of GSS bond analysts, who seek to ensure that instruments are rigorously assessed based on the quality and impact of the underlying projects financed by the bonds.

Through this framework, which is applied to both developed and emerging market green bonds, we aim to have a holistic and long-term view of issuers and projects we finance.

Finally, to reduce risk and attract private investors at scale in emerging markets, public-private partnerships can be envisaged. **Since 2017, Amundi and the International Finance Corporation (IFC) have partnered to invest in green bonds issued by the financial sector to finance the energy transition across emerging markets.**

What are the economic advantages for emerging market issuers to pursue green bonds compared to traditional bonds, and how does this affect the attractiveness of this asset class for asset allocators?

■ **Sergei:** In our view, green bonds offer an effective financing mechanism with benefits for both investors and issuers. For issuers, they can provide access to an additional and stable source of green financing. Green bonds may also allow issuers to match maturities with green projects, and enhance their sustainability profile among market participants and investors. **In some cases, issuers may benefit from the green premium, or "*greenium*", which refers to the potential yield advantage for issuers of GSS bonds over conventional bonds**, whereby investor demand for green assets may drive down borrowing costs.

For investors, green bonds can offer the potential of sustainable returns and the opportunity to have a direct impact in the *"greening"* of brown sectors.

Currency volatility and liquidity are key concerns in emerging market investments. How do you assess whether an emerging market green bond offers sufficient liquidity?

■ **Sergei:** When we invest in EM green bonds denominated in local currency, currency risk hedging is an active investment decision taken by the portfolio managers. In some cases, currency hedging is required to mitigate FX volatility and depreciation risks. In other cases, currency appreciation may be a strong contributor to positive investment performance.

Regarding hard currency bonds, we believe that the market is sufficiently deep and liquid. **Looking ahead, we expect annual EM green bond issuance to grow at a rate of 7.5% per year, to reach $156 billion in 2025[3].** This outlook – to which we attribute a 70% probability – assumes no reversal in investor demand for sustainable assets, alongside EM sovereign and corporate borrowers stepping up efforts to finance climate commitments. We expect further development and growth in this market, particularly from the private sector.

2. For more details, please refer to https://about.amundi.com/files/nuxeo/dl/d86ca73c-dcc6-437e-9f38-c57b18b338a1
3. For more details, please refer to the 2023 Amundi-IFC Emerging Market Green Bond Report

Article 3 disclaimer

IMPORTANT INFORMATION

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For Amundi ETF:

- Amundi Index Solutions, Luxembourg SICAV, RCS B206810, located 5, allée Scheffer, L-2520, managed by Amundi Luxembourg S.A.

- Amundi ETF ICAV: open-ended umbrella Irish collective asset-management vehicle established under the laws of Ireland and authorized for public distribution by the Central Bank of Ireland. The management company of the Fund is Amundi Ireland Limited, 1 George's Quay Plaza, George's Quay, Dublin 2, D02 V002, Ireland. Amundi Ireland Limited is authorised and regulated by the Central Bank of Ireland

Before any subscriptions, the potential investor must read the offering documents (KID and prospectus) of the Funds. The prospectus in French for French UCITS ETFs, and in English for Luxembourg UCITS ETFs and Irish UCITS ETFs, and the KID in the local languages of the Marketing Countries are available free of charge on www.amundi.com, www.amundi.ie or www.amundietf.com. They are also available from the headquarters of Amundi Luxembourg S.A. (as the management company of Amundi Index Solutions), or the headquarters of Amundi Asset Management (as the management company of Amundi ETF French FCPs, Multi Units Luxembourg, Multi Units France and Lyxor Index Fund), or at the headquarters of Amundi Ireland Limited (as the management company of Amundi ETF ICAV). For more information related to the stocks exchanges where the ETF is listed please refer to the fund's webpage on amundietf.com.

Investment in a fund carries a substantial degree of risk (i.e. risks are detailed in the KID and prospectus). Past Performance does not predict future returns. Investment return and the principal value of an investment in funds or other investment product may go up or down and may result in the loss of the amount originally invested. All investors should seek professional advice prior to any investment decision, in order to determine the risks associated with the investment and its suitability.

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A summary of information about investors' rights and collective redress mechanisms can be found in English on the regulatory page at https://about.amundi.com/Metanav-Footer/Footer/Quick-Links/Legal-documentation with respect to Amundi ETFs.

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