



# ESG Criteria and Capital Markets

by

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# Introduction

- Environmental, Social, and Governance (ESG) criteria have become increasingly important in capital markets
  - investors, companies, and regulators recognize the value of incorporating sustainability and ethical considerations into financial decisions.
- ESG criteria provide a framework for assessing the impact of a company's operations and policies on the environment, society, and governance structures.

# ESG criteria and the Maritime Industry

- ESG criteria are becoming increasingly significant in the shipping industry, influencing capital markets in various ways.
- The industry faces unique challenges and opportunities when integrating ESG principles.

# How ESG criteria are applied and their impact on shipping capital markets:

- **Environmental Criteria**

- The environmental impact of shipping is a concern, given the industry's substantial contribution to global greenhouse gas emissions, pollution, and resource consumption. Environmental criteria in shipping include:
  - **Emission Reduction:** The IMO has set targets to reduce CO2 emissions, leading to investments in cleaner fuels (e.g., LNG, biofuels), energy-efficient technologies, and new ship designs.
  - **Marine Pollution:** Efforts to minimize oil spills, ballast water discharge, and plastic waste are crucial. Compliance with MARPOL (International Convention for the Prevention of Pollution from Ships) is essential.
  - **Sustainable Practices:** Ship recycling and the use of eco-friendly materials in shipbuilding are also scrutinized

- **Relevance in Capital Markets:**

- **Green Bonds and Financing:** Shipping companies that adopt environmentally friendly practices can access green bonds and other sustainable finance instruments, often with favorable terms.
- **Investor Interest:** Institutional investors are increasingly prioritizing investments in companies committed to reducing their environmental impact, thus improving access to capital for sustainable shipping firms.
- **Cost of Capital:** Companies with poor environmental practices may face higher borrowing costs due to perceived risks, including regulatory penalties and the potential for stranded assets as regulations tighten.

# How ESG criteria are applied and their impact on shipping capital markets:

- **Social Criteria**

- The social aspect of ESG in shipping centers on the treatment of seafarers, community impact, and the industry's broader social responsibilities:
  - **Labor Practices:** Fair treatment of seafarers, including working conditions, wages, and mental health - a social issue. The COVID-19 pandemic highlighted challenges like crew changes and repatriation.
  - **Safety Standards:** Adherence to international safety standards to prevent accidents, injuries, and loss of life at sea is crucial.
  - **Community Engagement:** Shipping companies are also evaluated on how they engage with and contribute to the communities where they operate, including in ports and along shipping routes.
- **Relevance in Capital Markets:**
  - **Reputation and Risk:** Social performance can affect a company's reputation, which in turn impacts customer relationships, regulatory standing, and ultimately, its market value.
  - **Investor Preferences:** Investors are increasingly screening companies based on their social impact, particularly regarding labor practices and community engagement.
  - **Legal and Compliance Costs:** Companies failing to meet social criteria may face legal challenges, fines, or loss of licenses, increasing operational costs and reducing profitability.

# How ESG criteria are applied and their impact on shipping capital markets:

- **Governance Criteria**

- Governance in the shipping industry involves ensuring that companies have robust management structures, ethical practices, and transparency in operations:
  - **Corporate Governance:** Effective board oversight, clear accountability, and adherence to best practices in corporate governance are critical.
  - **Anti-Corruption Measures:** Shipping is susceptible to corruption, especially in dealings with port authorities and customs. Strong anti-corruption policies are necessary.
  - **Transparency:** Transparency in financial reporting, sustainability disclosures, and compliance with international regulations are essential for gaining investor trust.
- **Relevance in Capital Markets:**
  - **Access to Capital:** Companies with strong governance structures are more likely to attract investment, as they are perceived to be less risky.
  - **Investor Confidence:** Good governance practices ensure investor confidence, reducing the cost of capital and improving stock performance.
  - **Mergers and Acquisitions:** Companies with solid governance are often better positioned in mergers and acquisitions, which can be a crucial part of growth strategy in the capital-intensive shipping industry.

# How ESG criteria are applied and their impact on shipping capital markets:

- **Integration into Shipping Capital Markets**
- **Sustainable Shipping Finance:** Financial institutions and investors are developing products like sustainability-linked loans and green ship financing, which offer incentives for meeting ESG targets.
- **ESG Reporting and Disclosure:** Shipping companies are increasingly expected to disclose ESG-related risks and performance. This transparency helps investors assess long-term risks and opportunities.
- **Regulatory Pressure:** Regulatory bodies, particularly in Europe and Asia, are pushing for more stringent ESG compliance in shipping. Companies that align with these regulations can access capital more easily and at better rates.
- **ESG Ratings:** Shipping companies are being evaluated by ESG rating agencies (MSCI, Sustainalytics, FTSE Russell, Moodys, Refinitiv), influencing their attractiveness to ESG-conscious investors. These ratings affect stock performance and access to financing.
- **Shift in Investor Demands:** There is growing pressure from investors for shipping companies to demonstrate commitment to sustainability and ethical practices. This shift is leading to changes in how capital is allocated within the industry.

# How ESG criteria are applied and their impact on shipping capital markets:

- **Challenges and Opportunities**

- **Data and Measurement:** One of the key challenges in integrating ESG in shipping is the lack of standardized metrics and reliable data, particularly for environmental impact and social practices.
- **Technological Innovation:** Investments in new technologies, such as alternative fuels, electric ships, and digital solutions for efficiency, are both a challenge and an opportunity, requiring significant capital but offering long-term benefits.
- **Cost of Compliance:** Meeting ESG standards, particularly environmental ones, can be costly. However, companies that invest early in ESG compliance may gain a competitive advantage.
- **Long-Term Viability:** Companies that fail to adapt to ESG criteria may find themselves at a disadvantage, both in terms of access to capital and regulatory compliance, affecting their long-term viability.

# How ESG criteria are applied and their impact on shipping capital markets:

- **Future Trends**

- **Stricter Regulations:** The IMO and other regulatory bodies are likely to introduce stricter environmental regulations, pushing the industry further towards sustainability.
- **Increased Investor Scrutiny:** Investors are expected to increase their focus on ESG factors when evaluating shipping companies, leading to greater differentiation in capital costs.
- **ESG-Driven Innovation:** The push for ESG compliance will drive innovation in ship design, fuel technology, and operational efficiency, potentially reshaping the industry.

# How ESG criteria are applied and their impact on shipping capital markets:

## In sum

- ESG criteria are reshaping the shipping industry's relationship with capital markets by influencing investment decisions, cost of capital, and regulatory compliance.
- As the focus on sustainability and ethical practices grows, shipping companies that proactively adopt ESG principles are likely to enjoy better access to capital and a competitive edge in the global market.

# Green ship financing products

- **Global Market for Green Bonds in Shipping**
  - **Green Bonds:** The global green bond market, which includes financing for environmentally friendly shipping projects, is growing fast. By 2023, issuance of green bonds reached roughly \$600 billion, with a portion allocated to the maritime sector.
  - **Shipping-Specific Bonds:** e.g. Hapag-Lloyd and NYK Line raised hundreds of millions of \$ to finance energy-efficient vessels and reduce their environmental impact.
- **Sustainability-Linked Loans**
  - Sustainability-linked loans (SLLs) in shipping has seen significant growth. In 2022, the global market for SLLs reached over \$600 billion, with the shipping sector being a key beneficiary.
  - SLLs are tied to environmental performance indicators, such as CO2 emissions reductions, and often provide better terms (e.g., lower interest rates) if the borrower meets specified sustainability goals.

# Providers of green ship financing products

- **Nordea and DNB Green Financing**
  - **Nordea Bank and DNB** are among the leading financiers of green ship loans.
  - By 2023, Nordea issued over \$1 billion in green loans to shipping,
  - DNB's green loan portfolio for shipping has also grown significantly, with several hundred million dollars in green ship financing.
- **European Investment Bank (EIB)**
  - **EIB's** has committed billions of euros to green projects, including those in the maritime sector.
  - By 2022, the EIB financed more than €2 billion in green shipping projects, for construction of LNG-fueled vessels, hybrid ferries, and other eco-friendly ship designs.
- **Japan Bank for International Cooperation (JBIC)**
  - **JBIC** has been actively financing green shipping projects, particularly in Asia.
  - Has supported several large-scale projects, contributing to the financing of eco-friendly vessels and port infrastructure with commitments exceeding \$1 billion.

# Providers of green ship financing products

- **Green Shipping Program in Norway**

- Norway has been a leader in green ship financing, particularly through government-backed programs like Enova and the Green Shipping Program.
- Mobilized over NOK 1 billion (approximately \$120 million) in grants and financing to support development & adoption of green technologies in shipping.

- **Sustainability-Linked Bonds (SLBs)**

- SLBs are a newer financial product that links bond terms to sustainability performance.
  - Green loans are focused on financing specific environmentally beneficial projects, SLBs are broader financial instruments tied to overall sustainability performance metrics.
- Limited data on shipping-related SLBs, however, the broader market has seen fast growth, with more than \$130 billion issued globally in 2023.
- Shipping companies are beginning to tap into this market as they align financing with ESG goals.

# Developments of green ship financing products

- **ESG Investment Trends**

- The shipping industry has seen an increase in ESG investments, with institutional investors increasingly prioritizing companies that demonstrate strong ESG performance.
- According to a 2023 Bloomberg report, ESG assets are expected to exceed \$50 trillion by 2025, with shipping companies bidding for a share of this capital through green bonds, loans, and other financing mechanisms.

- **Challenges in Data Collection**

- Despite the positive trends, comprehensive and standardized data on green ship financing remains limited.
- The lack of standardized reporting and the relatively recent emergence of green financing products in shipping contribute to challenges in obtaining precise statistics.
- Some industry organizations, such as the **Global Maritime Forum** and the **Poseidon Principles initiative**, are working to improve transparency and data collection.
  - **Poseidon Principles**, in particular, aims to align ship financing with climate goals and has been tracking the carbon intensity of ship finance portfolios.

# Conclusions

- Financial institutions and investors are leading the way in developing and promoting green ship financing products.
- By offering loans, bonds, and other financial instruments tied to environmental performance, they are helping to drive the shipping industry towards a more sustainable future.
- These products are crucial for meeting regulatory requirements, reducing the industry's carbon footprint, and supporting innovation in maritime technology.



Thank you!