

The ECB and Alberta's oil production tax holiday

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AFII opines that the European Central Bank (ECB) should drop the province of Alberta's EUR denominated bonds (ticker ALTA) from its Eligible Marketable Assets (EMA) list. Alberta, a province of Canada, is rare in its commitments to climate change accelerating activities (Figure 1) but the latest headline "[Alberta grants tax holiday to oil producers](#)" (19 Oct, 2020) has a certain special extravaganza to it considering the state of climate change mitigation efforts in other parts of the world. The words of the [government of Alberta](#) are useful to understand the challenge:

"The responsible [sic!] development of oil sands is a key driver of Alberta's and Canada's economy. [...] Alberta's oil sands has the third largest oil reserves in the world, after Venezuela and Saudi Arabia."

Allowing Alberta bonds into the ECBs various operations is effectively a cost-of-capital subsidy. We believe it is simply irrational for European authorities to contribute such a subsidy. Alberta likely views the EUR market as a cheap funding source, e.g. the ALTA 0.5% 2025 bond currently trades at a yield of -0.26%. We opine that this would be higher if the bonds were ineligible for ECB operations. Please refer to the next page for more considerations around the ALTA bond curve.

Given that Alberta is not accounting for negative externalities, and that markets appear to not be pricing in these risks, **we believe the ECB could be right to refuse the issuer the eligibility status** in line with Ms Lagarde's comment:

"[M]ore needs to be done because it is probably the case that financial markets by themselves are not actually measuring the risk properly and have not priced it in" ([Financial Times](#), 14 Oct 2020)

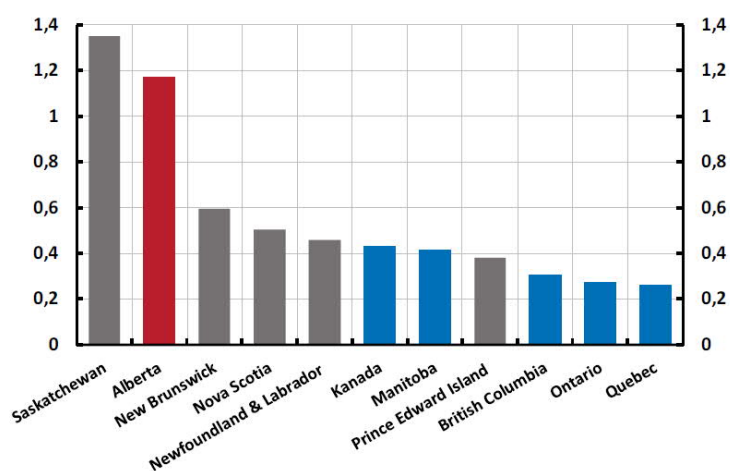
We note that **the Swedish central bank (Riksbank) took the decision to divest ALTA in November last year**, [Riksbank selling bonds for climate reasons](#), then focused on CAD paper in the FX reserve. Please note that ALTA bonds are not included in the CSPP program, but the EMA list has relevance for other purposes such as collateralization.

In short, **stopping out Alberta from the EMA seems like low-hanging fruit, in line with the AFII suggests in [An ECB Rapid Decarbonisation Plan](#).** For example, the carbon footprint of Alberta (pop. 4.7mn) is of in in the same ballpark as that of Italy (pop. 60mn), ~300MT CO₂e per annum.

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Figure 1 Direct emissions of GHGs, excluding land use. GHG (kT CO₂e)/BNP (mn USD) Reproduction from [Riksbank](#), original sources: Bloomberg, Government of Canada, UNFCCC and Statistics Canada.



Bond curve considerations

Table 1 highlights the securities in question and encompasses 8 bonds for a total nominal of more than €4.5bn, including three large benchmark issues. With the non-benchmark deals being ultra-long in maturity (20+ yrs), we note the considerable total risk sitting in these bonds, as they have such significant duration/DV01.

In all, we would - based on this - consider ALTA a fairly significant issuer in the EUR market. For the issuer, EUR bonds make up around 8% of total bond funding, but with a higher proportion in longer (+5yr) tenors.

We note that the last benchmark issue (ALTA 0.5% 04/25, €1.1bn) was issued as late as April, 2020. A quick review of the investor base of the benchmark bonds in Figure 2 indicates a fairly diversified investors base, where a number of investors are likely to be interested in reducing their carbon footprint and negative climate impact. Naturally, we are of the view that climate aligned investors should not contribute funding through purchasing ALTA bonds in primary or secondary market.

Finally, given the Swedish Riksbank's decision to disallow ALTA bonds in CAD, we would highlight the SEK2.5bn issue from 2019, where SEK2.5bn is considered quite a large issuance. Considering the low liquidity in the SEK bond space, an end-investor divestment from that bond could stir some interesting price dynamics, not least considering that the deal was syndicated by a non-domestic bank, with likely lower liquidity support capacity.

Figure 2. Alberta EUR outstanding bonds on the ECB Eligible Marketable Assets list and SEK outstanding bond (last row). Nominals in EURmn unless stated otherwise. 23 Oct 2020. Source: Bloomberg.

Ticker	ISIN	Issue date	Maturity	Nominal	Z spread	Coupon
ALTA 1.413% 03/50	XS2149308970	Mar-20	Mar-50	30	71	1.413
ALTA 0.5% 04/25	XS2156776309	Apr-20	Apr-25	1,100	22	0.5
ALTA 1.5% 04/50	XS2150179740	Apr-20	Apr-50	90	76	1.5
ALTA 0.925% 05/45	XS2167006357	May-20	May-45	70	61	0.925
ALTA 1.782% 12/40	XS1288314799	Sep-15	Dec-40	202	56	1.782
ALTA 1.15% 12/43	XS1492138729	Sep-16	Dec-43	435	55	1.15
ALTA 0.625% 04/25	XS1808478710	Apr-18	Apr-25	1,500	25	0.625
ALTA 0.625% 01/26	XS1936209490	Jan-19	Jan-26	1,250	28	0.625
ALTA 1.4025% 02/29	XS1944412318	Feb-19	Feb-29	SEK2500	40	1.4025

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Academic/technical papers

“The Green Bond Risk Premium: A Twin-Bond ULFP Approach”, SSRN working paper, Jul 2020. [Link](#).

“Credit alpha and CO2 reduction: A portfolio manager approach”, SSRN working paper, May 2017. [Link](#).

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