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Inside sustainable finance

TRANSITION FINANCE

Q1 2026

Introduction and global context
2026 began with a relatively slower but resilient sustainable finance market. As of Q1 2026, a cumulative total of US $6.99 trillion in aligned GSS+ bonds (including green, social, sustainability, and sustainability-linked bonds (SLBs) had been recorded globally, bringing the market close to the US $7 trillion milestone. Figure 1 shows the quarterly trend in Q1 2026.

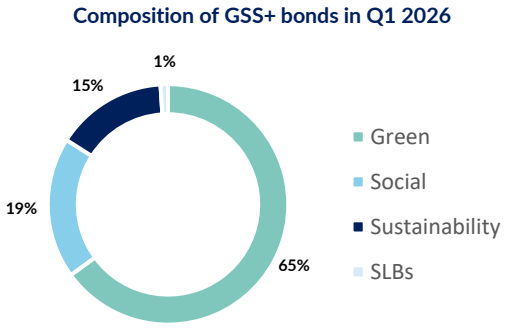

Fig 1: Quarterly issuer base of GSS+ bonds in Q1 2026

During Q1 2026 alone, aligned GSS+ issuance totalled US $230.3 billion. Compared to Q1 2025, aligned issuance declined by 9% on a like-for-like basis, reflecting a moderation in market activity following the record volumes seen in recent years.

In terms of instruments, green bonds continued to dominate the sustainable debt market, accounting for US $150.2 billion, ~ 65% of total aligned issuance during the quarter. Social bonds contributed US $42.9 billion (19%), while sustainability bonds accounted for US $34.2 billion (15%). SLBs remained a relatively small segment, with issuance of US $3.0 billion, representing ~1% of quarterly volume.

The issuer base of the global sustainable bond market remained diversified in Q1 2026. Government-backed entities accounted for 22% of total aligned issuance, followed closely by non-financial corporates (21%), development banks (19%) and financial corporates (19%). Sovereigns contributed 16% of quarterly issuance, reflecting the growing role of public-sector issuers in sustainable debt markets.

Austria emerged as the largest sovereign issuer during the quarter, raising US $8.2 billion through green bonds across multiple tranches. Mexico recorded a milestone by issuing a record US $6.9 billion in sustainability bonds, the highest quarterly sustainability bond issuance by the sovereign to date. In addition, Taiwan entered the sovereign sustainable debt market with its inaugural green bond issuance, reflecting the continued expansion and diversification of sovereign participation in sustainable finance.

Thematic focus: Transition finance

Transition finance is intended to mobilise capital for the decarbonisation of hard-to-abate sectors such as steel, cement, shipping, aviation, and chemicals. By supporting credible transition pathways, it enables emissions-intensive industries to adopt low-carbon technologies and business models while maintaining economic competitiveness during the transition to a net-zero economy.

Energy transition investment hit a record US $2.3 trillion in 2025 globally, up 8% from the prior year. The largest drivers were electrified transport at US $893 billion, renewable energy at US $90 billion, and grid investment at US $483 billion, signalling that capital is flowing into clean generation, but increasingly to the systems and end-uses that enable decarbonisation at scale. Key transition finance instruments currently supporting this shift are summarised in Table 1.

Instrument	Deployment context	Purpose
Climate transition bonds	Hard-to-abate corporates and sovereigns	Channel use-of-proceeds capital
Transition loans	Corporate borrowers in high-emission sectors	Provide structured bank financing
Sustainability-linked bonds (SLBs)	Cross-sector issuers	Link cost of capital to emissions or sustainability KPIs
Sovereign transition bonds	Governments	Finance national decarbonisation
Blended/MDB-anchored transition finance	EMDEs and frontier markets	Crowd in private capital

Table 1: Existing transition finance instruments

Most forms of transition finance can be classified under two categories. A general purpose transition investment where funds are not ringfenced, but engagement towards a transition activity is applied on the basis of the influence the investor has over the asset. Or a specific-purpose transition investment where the use of proceeds of the funds provided are for delivering a certain transition activity or outcome.

Key principles of transition linked instruments:

Intentionality (Pre or during investment): Transition objective is made clear and built into investment process

Accountability (During or post investment): Transition outcomes are delivered and level of success is

The relevance of transition finance has grown sharply since hard-to-abate sectors such as steel, cement, aviation and shipping account for a substantial share of global emissions. According to estimates, broader "hard-to-abate" industries such as aviation, trucking, steel, cement, collectively contributes ~ 40% of global emissions. These sectors are capital intensive, trade exposed, and reliant on technologies that are still unevenly mature, thereby making green finance alone insufficient. Therefore, transition finance fills this gap by financing companies and projects that are not yet green, but are moving towards lower emissions through credible transition pathways.

Policy and regulatory developments

The transition finance landscape in 2026 has been defined by growing scale, increasing maturity, and the continued development of more structured transition finance frameworks. The emergence of guidance, especially from International Capital Market Association (ICMA), the Loan Market Association (LMA), and aligned regulatory standards in late 2025 enabled transition financing under a use-of-proceeds structure with a recognised label and structured safeguards.

In addition to this, the European Commission has proposed to introduce a 'transition' product category for funds investing in entities or projects that are not yet sustainable, but on a credible transition path. Consequently, 2026 marks the beginning of steady expansion in explicitly labelled transition issuance, particularly in hard-to-abate sectors. The cumulative effect is a market that is moving to a more structured, label-led, and disclosure-driven phase.

This shift toward a disclosure-driven phase has been reinforced by the steady global uptake of the International Sustainability Standards Board (ISSB) standards, with 28 jurisdictions having adopted IFRS S1 and S2 on a voluntary or mandatory basis as of April 2026, and a further 12 in the process of finalising adoption.

Additionally, Japan's Financial Services Agency mandated ISSB-aligned sustainability disclosures for listed companies from February 2026. Companies with market capitalisation of over US $18 billion (¥3 trillion yen) listed on the Tokyo Stock Exchange's Prime Market will be required to start publishing sustainability reports for the fiscal year ending March 2027.

The EU Carbon Border Adjustment Mechanism (CBAM) definitive phase came into effect with full financial compliance for covered imports, including cement, iron and steel, aluminium, fertilisers, electricity, and hydrogen, acting as an external forcing function for hard-to-abate transition globally.

Overall, transition bond issuances are forecasted to grow to US $40 billion, nearly double the record issuance of US $21 billion reached in 2024. This near-doubling reflects both, demand from hard-to-abate sectors and growing investor comfort with explicitly labelled transition instruments. The market is now characterised by a more diversified issuer base, spanning sovereigns, development finance institutions, and corporates across emerging markets and developing economies (EMDEs).

Case studies

1. Japan Green Transformation (GX) economy transition bond

Japan has pledged to reduce its GHG emissions by 46% by 2030 (from 2013 levels) and achieve carbon neutrality by 2050. Japan ranks fifth in energy consumption and is the fourth largest economy, globally. As a result, its transition towards net zero will be significant for global efforts to achieve the Paris Agreement targets.

Japan has positioned itself at the frontier of sovereign transition finance through the Japan Climate Transition Bond Framework, the world's first government-labelled transition bond framework. The framework was developed to operationalise Japan's broader GX strategy, integrating fiscal policy, carbon pricing, and industrial transformation into a single financing architecture.

Instrument

The Japan transition bond market stands at US $35.8 billion (JPY 5.37 trillion) currently, mainly comprised of the government's Japan Climate Transition Bonds (JCTBs). The most recent issue of the bonds achieved 4x bid to cover ratio, despite market volatility. Cumulative issuance under the GX sovereign bond programme reached approximately US $26 billion (JPY ¥4.2 trillion) as of March 2026, making it the largest sovereign transition bond programme globally.

The 2023 GX Promotion Act authorised US $124 billion (JPY ¥20 trillion) of issuance over 10 years, intended to catalyse US $935 billion (JPY ¥150 trillion) in combined public-private green and transition investment and accelerate Japan's path to carbon neutrality by 2050.

The Ministry of Finance acts as the issuer, with Ministry of Economy, Trade and

Investment and the specialised GX Implementation Council oversee project eligibility and allocation decisions. Proceeds finance a portfolio of decarbonisation and transition projects spanning hydrogen, ammonia, next-generation nuclear, energy efficiency and industrial transformation.

The framework explicitly accommodates technologies that are not yet classified as green under stricter taxonomies but are considered essential to Japan's industrial decarbonisation pathway. Repayment is linked to revenues from the GX-ETS and a planned fossil fuel surcharge, creating a feedback loop between carbon pricing and transition financing.

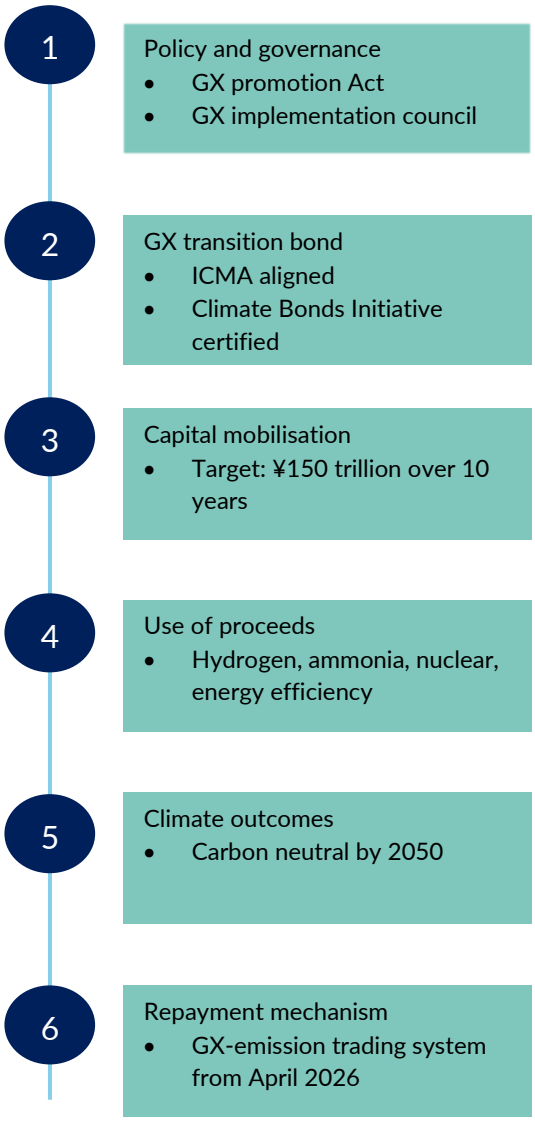

Fig 2: GX strategy

Impact

The GX bond programme has de-risked early-stage investment in technologies that fall outside conventional green labels but are essential to Japan's industrial decarbonisation pathway. Crucially, the structural link between bond redemption and future carbon-pricing revenues, via the GX Surcharge from 2028 and ETS auctioning from 2033, has demonstrated how a sovereign can embed the polluter-pays principle directly into its debt structure.

2. Transnet freight decarbonisation and corporate sustainability programme

South Africa's freight sector is a critical component of the country's decarbonisation strategy, given its central role in supporting the commodity export economy. It has significantly contributed to transport-related emissions, particularly through road freight. Its transformation is closely aligned with South Africa's Just Energy Transition Investment Plan (JET-IP) 2023-2027, which identifies nearly US $98 billion in financing needs across key transition sectors.

As the state-owned operator of rail, ports, and pipelines, Transnet is pivotal to this agenda. Investments in rail and port infrastructure can shift freight from higher-emitting road transport to lower-carbon rail, improve logistics efficiency, and strengthen trade competitiveness.

Instrument

As part of the JETP-IP, the Transnet company received US $346 million transition-linked loan (€300 million) from the Agence Française de Développement (AFD). This loan fulfils France's US $1.1 billion (EUR €1 billion) commitment to the JETP announced at COP26.

The transaction represents a layered transition finance model, combining bilateral development finance with the strategic priorities of a state-owned enterprise and a national just transition framework.

The program consists of three distinct layers:

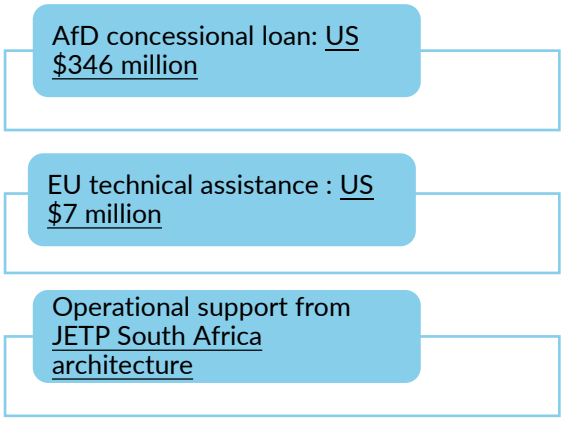

Fig 3: Instrument layers

It demonstrates how transition finance can be deployed in EMDE infrastructure sectors where outright green labelling would be premature, but where credible, plan-anchored financing can unlock meaningful emissions reductions.

Disbursements are conditional on Transnet achieving certain Key Performance Indicators (KPIs):

Key Performance Indicators:

Fig 4: KPIs of the Transnet freight decarbonisation and corporate sustainability programme: Railway Gazette

The loan is aimed at strengthening Transnet's operational sustainability and advancing the decarbonisation of South Africa's freight sector. It focuses on enabling a transition to a low-carbon operating model aligned with South Africa's JET-IP, and enhancing the company's long-term financial sustainability. By embedding the loan within Transnet's wider corporate reform programme, the structure ensures that financing is tied rail rehabilitation, port upgrades, and energy transition initiatives across Transnet's network.

Relevance

By routing capital through a state-owned enterprise rather than the sovereign balance sheet, it unlocks decarbonisation in freight, ports, and green hydrogen logistics, where green labelling would be premature, but transition financing is essential. It also signals a larger role of the JETP model in 2026, with sustainability-linked structures, KPI-based disbursement, and bilateral DFI–EU grant blending providing emerging pathways for transition finance.

3. QNB Türkiye climate transition bond (CTB)

Türkiye's revised Nationally Determined Contributions (NDCs) commit to a 41% reduction in GHG emissions by 2030. One of the key moves to achieve those goals was by issuing a climate transition bond in December 2025. This issuance is novel as it is the first under the new ICMA guidelines, making it's the first 'transition-labelled' bond. Hence, the transaction serves as a market-shaping reference point for subsequent issuers in EMDEs.

Instrument

QNB Türkiye issued the world's first CTB issued by a financial institution worth US $100 million with IFC as the sole investor. The instrument is a 5-year, use-of-proceeds CTB, with at least US $50 million designed to support low-carbon and resilience investments across Türkiye in steel, cement, aluminium and fertiliser sectors.

CTBs need to be anchored to a credible transition plan, demonstrate alignment with recognised decarbonisation pathways. Through its engagement in ICMA's Climate Transition Finance Working Group, IFC helped shape the latest climate-transition finance standards. This bond utilises use-of-proceeds to finance eligible transition activities under QNB's Sustainable Finance and Product Framework. Under ICMA's "meet or explain" safeguards, the issuer needs to also show that no viable low-carbon alternative exists and that any risk of carbon lock-in is disclosed and mitigated, with annual reporting on allocation and progress.

Impact

The bond is expected to unlock long-term capital for emissions-intensive industries that have traditionally struggled to access sustainable finance, enabling investments in cleaner technologies, energy efficiency, and climate resilience. By reducing financing barriers for first-mover transition projects, it can accelerate emissions reductions across Türkiye's industrial sector while encouraging similar issuances by other financial institutions, thereby multiplying its impact beyond the initial US $100 million.

By embedding transition planning as essential element of the bond framework, this transaction sets a benchmark for other Turkish banks and accelerates the country's financial sector towards the Paris Agreement goals.

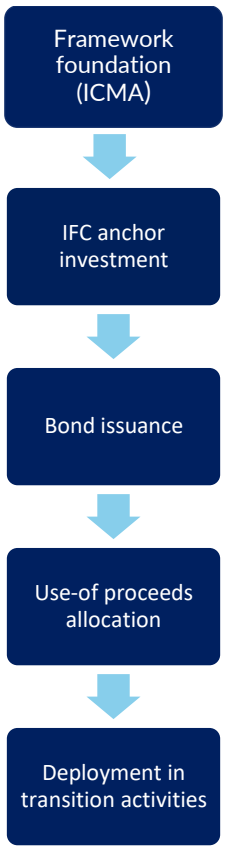

Fig 5: Structure of the QNB Türkiye CTB

Conclusion

The current transition finance landscape underscores that it is a structured, standard-led segment of global sustainable finance. The combination of ICMA's transition labels, jurisdictional regulation such as CBAM and the SFDR review, and sovereign leadership through programmes such as Japan's GX bonds has shifted the conversation from whether transition finance is credible, to how can we ensure this scales rapidly. With approximately US $30 trillion in incremental investment required across hard-to-abate sectors, the coming quarters would be defined by how effectively issuers, standard-setters, and how investors translate this architecture into deployable capital and verifiable emissions outcomes.