THE BOND BUYER

More issuers are investing to reduce climate risks

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Wildfires on the West Coast and a seemingly unending train of hurricanes threatening the coasts along the Atlantic Ocean and the Gulf of Mexico provided an unmistakable sense of urgency as sustainable finance leaders from around the world converged online last week for the first virtual Climate Week NYC.

But the concerning headlines about climate-related natural disasters (and the risks they pose to essential public infrastructure and the credit quality of the municipal bonds that finance it) were also met with early signs that municipal issuers are embracing the challenge to re-think their capital plans with resilience in mind.

As that trend takes hold, the green bond market is likely to be called upon to help them realize those initiatives. At Build America Mutual, we're acting to support that shift by expanding our BAM GreenStar assessment program, which provides a third-party verification of a transaction's alignment with the International Capital Market Association's Green Bond Principles and has verified more than 100 municipal bond sales worth more than $1.5 billion.

One of Climate Week's signature events — an online discussion with California State Treasurer Fiona Ma sponsored by Nasdaq — demonstrated that both issuers and investors see benefits from the continued growth in the labelled green bond market. Treasurer Ma delivered an update on the state's efforts to adopt a green bond framework and sell green bonds to pay for capital projects that align with the ICMA Green Bond Principles … and the audience provided feedback that when it comes, a State of California green bond issue is likely to find a ready audience among investors. A poll of participants revealed that 48% of participants said a "lack of supply" is the most important constraint on their green bond purchases, and a majority said the market could support more than $700 billion of global green bond issuance per year (last year's record volume was just $225 billion).

Those data points echoed the trends we’ve been observing in BAM GreenStar transactions throughout the summer: Even as the market overall was dominated by refunding transactions, we saw a significant increase in the number of issuers selling larger, new-money bond sales to finance projects that represent a departure from their “business as usual” capital plans.

A recent BAM GreenStar bond issue sold by the Fort Bend County Levee Improvement District No. 7 West of Houston is a good example: Property owners within the LID are facing significant and increasing risks due to erosion along the banks of the Brazos River, which borders the district.

The erosion was a relatively new phenomenon, emerging after severe storms between 2015 and 2017, including Hurricane Harvey. An engineering study showed that the initial damage was accelerating subsequent erosion, due to the “helicoidal” flow of currents within the river. The district’s response will both stabilize the riverbank and “re-train" the river’s flow to the center of the original channel, protecting both its residents and downstream communities.

Like many municipal issuers, the District did not undertake the project with green bonds in mind — it was focused on solving the problem. But as the transaction came to market, BAM was able to review public documents and the district’s commitment to ongoing reporting under the terms of a separate grant to confirm that these bonds align with the Green Bond Principles and provided an appropriate level of transparency to investors who want to make sure their money is spent as intended.

Since BAM GreenStar only verifies U.S. municipal bonds, our approach to verifications was developed with the recognition that municipal policymakers, from elected officials to civil engineers and public works directors, frequently embed best practices in sustainable planning and environmental stewardship into their capital plans — and that state and regional oversight bodies provide an additional layer of accountability.

Our underwriters start their reviews by leveraging that existing work whenever possible: So we can confirm an issuer’s process for project evaluation and selections meets the ICMA’s guidelines while also minimizing the burden on municipal finance officers, who are already managing dozens of moving parts in any bond sale.

The new changes to the BAM GreenStar program were similarly developed with the specific needs of municipal issuers in mind and will remove additional obstacles to labelled green bond issuance. We are offering verifications to all of our member issuers, whether their new-issue sales will be insured, and we are easing the post-issuance compliance burden for participating issuers — we will take on the responsibility for post-issuance monitoring and reporting as part of the regular surveillance of our insured portfolio.

As a result, BAM members and their underwriters and municipal advisors can include a no-cost third-party verification in their sales efforts, even before making the call about using insurance on a new-issue, and they will not have to assume responsibility for ongoing reporting.

Ultimately, increasing the volume of labelled green bonds is a necessary prerequisite for the nascent market to demonstrate a consistent pricing advantage. We look forward to working with BAM's member-issuers to make sure deserving projects receive attention from the widest possible range of investors.

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