

THE BOND BUYER

Commentary How climate change threatens to leave water bonds high and dry

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Hurricane Florence caused record flooding at water and wastewater plants in North Carolina. [Saltwater intrusion](#) from rising sea levels is wreaking havoc on Florida's water supplies. The nearly two decades of drought afflicting the Colorado River Basin will soon require [Southern California](#) to cut its draw from the river by as much as 8%.

Climate resiliency is becoming an increasingly material issue for utilities that manage water infrastructure and investors who buy the bonds to finance these assets. As climate risks rise, utilities and their bond buyers must address growing questions about the long-term resilience of existing and planned water infrastructure, to prevent these investments being left high and dry.

Last fall, [Moody's](#) warned New Orleans, Miami and other Gulf Coast cities to prepare for climate impacts or risk a downgrade on their bond ratings. In July, a University of Pennsylvania [study](#) warned of broader credit rating downgrades for all coastal communities that do not manage flooding and rising sea level risks.

“What are we going to do when sea level rise is constantly battering cities? Declare a chronic emergency? We're talking about hundreds if not thousands of cities at risk,” said UPENN's John Miller, who wrote the “Credit Downgrade Threat” report.

These actions linking credit worthiness to climate resiliency are an important wake up call to water utilities that they must prepare for climate change.

And momentum is clearly growing. Among the more recent breakthroughs is [new guidance](#) issued this spring by the National Federation of Municipal Analysts (NFMA) regarding utility disclosures. The guidance asks for stronger disclosure on potential climate impacts to physical assets, water supplies and revenue streams. It also asks utilities to share more about their plans to protect critical

water sources as well as planned conservation measures to ensure water availability.

The NFMA's *Recommended Best Practices in Disclosure for Water and Sewer Transactions* guidance follows in the wake of an evaluation tool Ceres has developed to help bond investors assess the resiliency of water utility-related investments. The [Water Risk Framework for Municipal Water and Wastewater](#) is part of a new open-source water risk toolkit created in collaboration with a group of over 40 asset managers and owners.

Another development that will shape the future of the municipal water bond market is the finalization of new [water infrastructure criteria](#) for green bonds. The new standard, which use specific scoring criteria to rank water projects on climate adaptation and environmental impacts, come as the [green bond market](#) is taking off globally, hitting a record \$162 billion in 2017. Several utilities have already issued [\\$1.5 billion of green water bonds](#), including San Francisco, Washington, D.C., and Cape Town, South Africa.

Still another development is a recent change by the Governmental Accounting Standards Board [to its guidance for bond financing for distributed infrastructure investments](#). The clarification makes clear that green roofs, smart meters, water efficient devices and other water-saving measures are assets that can be capitalized and debt-financed by water utilities. Having this financing flexibility will make it easier for utilities to deploy these types of assets at far greater scale.

The bottom-line takeaway should be clear: as climate impacts create bigger challenges for the water sector, it is incumbent on bond investors to understand these risks — and for utilities to disclose and plan for them.