

THE BOND BUYER

Climate change, a rising tide affecting the muni market

By

Sarah Wynn

Published

January 08 2019, 12:45pm EST

WASHINGTON — Portfolio managers are feeling the heat when it comes to investing in bonds that could potentially be affected by climate change.

Climate change has long been a point of political and social contention, and investors are throwing caution to the wind when making important bond transactions, while using a green thumb to do their part.

Eric Glass, portfolio manager at Alliance Bernstein, says not enough industry professionals are taking notice of changes in the climate.

“Personally, I don’t believe the industry itself has sort of taken the time to grapple with that issue and I don’t think that there are too many other portfolio managers who are thinking in those terms,” Glass said.

He said some portfolio managers talk about water sanitation, electric and utilities, but aren’t necessarily paying attention to the climate change aspect of it.

“How are we conserving water, how are we transitioning from fossil fuels to renewables,” he said. “Are we using our influence as investors to nudge and promote such investments?”

However, municipalities and rating agencies aren’t paying attention to long-term assets, Glass said. Assets such as new systems for renewable sources of energy like solar are long-term assets.

“Most politicians, most mayors, most governors unfortunately on some level are thinking more short term for the next election cycle, the next economic cycle and viewing these things more as a cost as opposed to an investment,” Glass said.

Glass said many energy plants need to be retired and people need to invest in more sustainable energy.

“So hopefully, we’ll be able to move the needle from an industry perspective,” Glass said.

With his municipal impact portfolio, Glass evaluates credits based on environmental and social aspects such as sea level rise because he considers them risks going forward. Glass said he considered investing in American Samoa in the South Pacific because he invests in largely underserved and marginalized communities. However, it historically has its fair share of storms.

“Climate change is a prominent issue that they need to address in some way, shape or form,” Glass said. “They need to become more resilient in the face of climate change and they need to do whatever they can to mitigate the impacts of climate change.”

As a portfolio manager, he is wary and so restricted purchases to five year timeframes instead of purchasing longer-term debt.

“I am not willing to take climate change risk for 20 years out for a place like American Samoa,” he said.

The same goes for John Mousseau, president and chief executive officer at Cumberland Advisors in Sarasota, Fla.

With his clients, Mousseau said he discusses climate and infrastructure, especially when it comes to residential developments along the coast.

“Just as a matter of policy, we generally try to avoid credits that are particularly vulnerable along any coasts,” Mousseau said.

Instead, he believes in diversifying by owning county bonds or multiple types of utility bonds, as opposed to smaller general obligation bonds that could get wiped out by a hurricane.

Mousseau said there will be an increase in green bonds — bonds used specifically for climate and environmental projects —and more institutional clients are starting to ask for them.

“I think there’s a heightened sense of people wanting to be involved in investments that benefit the environment and I think that grows every year,” Mousseau said.

Millennials, in particular, have shown interest in green bonds, which could cause a rise in issuance.

Development has increased in energy market countries and Mousseau believes green bond initiatives will become more important.

“All I’m saying is that the idea of green bond initiatives is certainly not stopping here,” he said.

Disclosure

In early 2018, ExxonMobil countersued California local governments alleging that contradictions between the municipalities’ bond documents and their lawsuits against oil companies could be considered securities fraud.

ExxonMobil said they failed to disclose risks such as rising sea levels in their bond offerings.

Kevin White, a lawyer at the law firm of Butler Snow,, said he has noticed more disclosure around climate change in Virginia when it comes to sea level rise and its effect on utility, water and sewer and storm water bonds. White represents financial institutions, hospital and healthcare organizations, and higher education institutions, among others.

He sees issuers disclose climate change information in general obligation bond statements and governmental enterprise bonds, but says it's lacking in private activity bonds.

"I do a lot of work with hospital systems and educational institutions and I don't think I've seen any climate change related disclosure in private activity bond transactions yet," White said.

He characterized climate change disclosure as an evolving area of disclosure.

Economic effect

Rising global temperatures and sea levels put credits at risk and cities such as New Orleans saw a significant decline in revenue, according to a 2017 Moody’s report. The city’s population in 2004 was about 455,000 and assessed valuation and total sales tax revenue were \$16.7 billion and \$150 million, respectively.

In 2006, after Hurricane Katrina, the population fell to 223,000 and assessed valuation and total sales tax revenue decreased to \$12.9 billion and \$115 million. The city’s population has never fully recovered, according to the report.

Mousseau said Sarasota is seeing its own threat to the state's vital tourism revenue — red tide. Natural algae increases partly because of warmer water due to climate change and becomes red and chokes off oxygen in the water, killing the fish.

It becomes a cycle, Mousseau said. The red water smells, deterring tourists, tourism decreases leading to less revenue filtering through hotels and

restaurants. He expects the state will play a bigger role in the future to combat climate change.

"There is a tipping point to this stuff," he said.

Mousseau referenced a saying from Speaker of the House Tip O'Neil — "all politics are local."

"In other words, not that there's not national issues, but what people really care about are issues that affect them locally," Mousseau said.