Bond Case Briefs

Municipal Finance Law Since 1971

Green Bonds Sell Big in 2014 as Finance Bids to Help Climate.

(Reuters) – A "green" bond market has taken root this year, with municipalities and corporations issuing new environmentally-focused bonds and money managers jumping in to buy them.

But it's too soon to tell whether all the new activity – less than a sliver of the $91 trillion worldwide bond market – will send much new money to projects like efficient buildings and better water systems.

Instead, the new bonds reflect the complexities of using finance to address issues like climate change. While the sale of notes termed green bonds tripled to $35 billion worldwide in 2014, many are bonds that might have been sold anyway without the label, and which trade at terms comparable to non-green bonds.

Nor is it clear the new bonds are "green" in the environmental sense that investors may expect, and issuers face only voluntary standards so far.

Participants say that to avoid the impression that green bonds are just a marketing ploy, they still need to show more corporate treasurers and investors the bonds can make it easier to fund projects, a corner they have not yet turned.

"If people think this is just to raise the flag, it's not going to last long," said Christopher Flensborg, Head of Sustainable Products and Product Development for Skandinaviska Enskilda Banken AB, the Swedish bank that's the world's largest underwriter of green bonds.

Still, the spike in new activity shows some success to date, with new issuers and new buyers. Green bonds used to come exclusively from AAA-rated organizations like the World Bank; the last year has seen rising issues of green bonds from municipal issuers as well as some from corporations that are rated junk.

On the buy side, State Street Corp has filed a registration with the U.S. Securities and Exchange Commission to run what could be the first green bond index fund. Also, since July Bank of America Corp, Standard & Poor's and Barclays MSCI each have launched new green bond indexes that may form the basis of future mutual funds and exchange traded funds.

Corporate and municipal issuers started issuing bonds they labeled as "green" in earnest last year, when they realized that they could pull in some new buyers who wanted to invest environmentally.

"We thought the worst thing that happens is we get more people interested in our bonds" said Alan Westenskow, a Zions Bank vice president who works with municipal issuers. He advised the Utah Associated Municipal Power Systems on a $21 million offer this month to pay for systems to turn waste heat to electricity. The offering, made in several sections, pays a coupon ranging from 3 percent to 5 percent.

Spanish clean energy company Abengoa Greenfield, a unit of Abengoa SA issued its first high-yield green bonds in September – a 500-million-euro issue in all. A representative said “90 percent of our projects qualify as green projects, so why not issue a Green Bond?”

Still unclear is how much extra demand the green label creates. The Abengoa representative said the company didn’t have information on the extra demand. A spokesman for Bank of America, which underwrote the Utah bonds, said executives there would not comment on demand.

JUNK GREEN BONDS

In August 2014, the first wave of corporate junk green bonds entered the mix, when an affiliate of Princeton, New Jersey, power producer NRG Energy Inc sold $500 million of senior notes to pay for the purchase of the Alta Wind Energy Center, a wind farm in California. Abengoa followed suit, bringing the green high yield market to $1 billion.

Corporate issues now make up 14 of the 51 green bonds tracked in Bank of America’s green bond index, and have driven down its average rating to AA2 from AAA, according to a BofA Merrill Lynch research report.

At $1.98 billion, green muni bonds themselves are just a fraction the “green” market, possibly because many muni issues have traditionally backed environmental projects and find investors even without the green label.

“At the end of the day, a bond is still a bond whether it’s dubbed as ‘green’ or not,” Eva Rippeteau, associate director at Fitch Ratings, said in an emailed analysis sent after the Metropolitan Water Reclamation District of Greater Chicago came to market this week with a $300 million green bond, with a coupon ranging from 2 percent to 5 percent. “In many cases, these bonds are funding the same projects that a regular bond would.”

Orders for a recent $350 million green bond sale by Massachusetts exceeded $1 billion, like many other over-subscribed municipal offerings. One buyer, Charles Hill, portfolio manager of T. Rowe Price’s $3.9 billion Summit Municipal Intermediate Fund, said he has never had client requests for green bonds specifically, but bought the Massachusetts bonds because he liked them for traditional criteria like their intermediate duration, and their 5 percent coupon, comparable to that of similar non-green bonds.

GREEN CONSCIOUS

To be sure, the entire movement isn’t about labeling. A spokeswoman for NRG Energy said it used the term “to be able to target an incremental universe of investors who are more green conscious and to differentiate ourselves from other issuers.”

Steve Liberatore, a TIAA-CREF fund manager who oversees $6 billion in bond products that use social or environmental criteria to pick investments for clients concerned about the use of their money, said he skipped the NRG bond because the company also has natural gas operations. He aims to avoid fossil fuels.

“What we’re seeing is a shift in the ability of the investor to link up directly with the projects” focused on sustainability, he said.

Interested investors and issuers are willing to give it time to grow, and to improve their standards. The Climate Bonds Initiative, a London nonprofit that promotes investments to reduce carbon emissions, estimates 39 percent of green bonds sold since 2013 were issued without an independent review of how green they are. Many institutional buyers do have internal standards for what kinds of projects green bonds can back.

Catherine Roy, Calvert Investments' chief investment officer for fixed income, said she expects no slowdown. "There are still trillions of dollars of capital needed to address a wide range of global environmental challenges," Roy said.

Reuters
By Ross Kerber and Hilary Russ
December 18, 2014 1:05 AM

(Reporting by Ross Kerber in Boston and Hilary Russ in New York. Additional reporting by Francesca Landini in Milan and Jose Elias Rodriguez in Madrid. Editing by Linda Stern and John Pickering)