Bond Case Briefs

Municipal Finance Law Since 1971

US Green Finance: A Clearer Year Ahead.

The US green finance surge continues regardless of federal government, argues S&P Global Ratings' Michael Ferguson

The American green bond market has been stepping up. Last year, dollar-denominated green issuance grew substantially: self-labelled US municipal bonds reached $10.4bn, a 43 per cent increase on 2017. Importantly, American municipal issuance alone accounted for 34 per cent of the global sub-sovereign issuance, and included 10 first-time issuers, according to the Climate Bonds Initiative (CBI).

This expansion of the marketplace could just be the beginning. Forecasts suggest that issuance by US municipalities could top $15bn in 2018 – representing an increasingly diverse and proactive group of sub-federal actors, which also extends to large corporations. On this evidence, state-level climate action is significantly bolstering the country's green marketplace even amid uncertainty at the federal level.

In turn, this is driving forward a decarbonisation agenda, despite the current federal disinclination to pursue comprehensive carbon reduction policies. Indeed, uncertainty about US regulatory policy may have hitherto contributed to limited growth in corporate green bond issuance. The US' revised tax code, however, has provided some market clarity, at least for now.

It ensures that both the production tax credit (supporting wind) and the investment tax credit (supporting solar) will continue. So, corporate taxpayers can still benefit from the credits, which have propelled investment in renewable assets in the past. And though the credits' retention was a surprise to many, it has revealed a clear bipartisan support for renewable energy in the US, possibly contributing to a continuing a surge in green finance.

Continuing tax credits

The production tax credit (PTC) has historically supported wind power generation. With its help, America's wind capacity quadrupled between 2007 and 2014. Then, in 2015, the market suspected (incorrectly, with hindsight) that the PTC would be excluded from future budgets. As a result, installed wind capacity surged to capture the credits before expiry. When the credit was omitted from early versions of the 2017 federal budget – along with the investment tax credit (ITC) for solar – the market gave pause.

However, the final version of the tax reform bill signed into law by President Trump in December 2017 continued the credits. Many believe that the bill could substantially increase the federal deficit, based on non-partisan estimates. Yet, in a bill passed without a single democratic vote, the preservation of both the PTC and the ITC speaks to the enduring value of the credits as tools for spurring renewable development.

With the phase-out of the tax credit temporarily avoided, S&P Global Ratings expects that renewable financing, especially corporate power purchase agreement (PPAs), will continue to grow. Although

growth will be spurred in part by diminished costs, we don't expect an immediate surge in financings as experienced in 2015. But with a clearer outlook ahead, the US renewable energy market will likely enjoy a steadier growth trajectory through the beginning of the next decade.

Worth a little less?

That being said, the revised tax code may have an indirect impact on the value of the PTC and ITC, thereby presenting a possible new market dynamic. A lower corporate tax rate – with the marginal percentage down to 21 per cent from 35 per cent – could undermine the value of some tax equity investments. In turn, this may influence issuers' decisions about whether to use tax-exempt municipal issuances, corporate debt, or project finance debt.

Further, in the absence of a federal policy on climate change, we're not likely to see the pricing signals associated with a carbon tax or emissions trading, and consequently the financeability of projects could be dependent on both state level policies (including RPS) and the value of these tax credits. Given the limited pool of equity investors, revisions to the tax code may also have ramifications for the green marketplace – and alter how such projects are funded.

Infrastructure goes green

Regardless, the funding will have to come from somewhere. America's infrastructure needs are vast – with green finance increasingly used to fund improvements. According to the US Environmental Protection Agency, the country's water, wastewater and irrigation systems require over $630bn of investment through to 2033 in order to bring them up to modern standards. And there is broad consensus on Capitol Hill that the country's aging infrastructure, which has been underfunded for decades, is in need of an overhaul.

The White House has recently proposed over $1tr in infrastructure investments, in addition to the $200bn included in the 2018 budget. However, much of the funding for these projects – about 75 per cent according to the Council on Foreign Relations – will have to come from state and municipal budgets, as it has done for most of the past century. This, coupled with heightened sub-federal decarbonisation and adaptation initiatives, makes more green financings possible nationwide.

In turn, S&P Global Ratings anticipates another banner year for US green bond issuance – and the wider green finance marketplace. Propelling the market will likely be a mixture of renewable-backed issuances and others to repair, or even replace, some of the country's infrastructure. While estimates for green bond issuance vary wildly, and can hinge on a bevy of market and political conditions, it is clear that green instruments have firmly secured their place within the US financial landscape, and their prominence will only grow as investors become more sensitive to climate concerns.

businessgreen.com

Michael Ferguson, S&P Global Ratings

09 March 2018

Michael Ferguson is director of US energy infrastructure at S&P Global Ratings

Copyright © 2026 Bond Case Briefs | bondcasebriefs.com