
Muni Bonds Gain Traction for Climate and Social Change.

KEY POINTS

- With built-in tax benefits and relatively low default risk, municipal bonds have grown more popular amid the threat of tax hikes.
- There's also a surge in interest for muni bonds among impact-driven investors seeking funds for climate and social change.
- Experts at the CNBC Financial Advisor Summit covered what to know about these muni bond trends.

Many investors already know about the tax benefits of municipal bonds — also known as muni bonds or "munis." Now these assets have also become popular among those who want to have an impact on climate and social change.

In addition to tax savings and relatively low risk, muni bonds may be attractive to those seeking funds in areas such as renewable energy, clean water, low-carbon transportation or infrastructure.

The muni bond market increased by $474 billion in 2020, with $27.6 billion issued for green, social or sustainable bonds, more than double the numbers from 2019, according to S&P Global Ratings.

"We expect growth in the green bond market to also be driven by a renewed focus on climate change and the aging state of the nation's infrastructure," said Laura Levenstein, chief risk officer at Build America Mutual, speaking at the CNBC Financial Advisor Summit on Tuesday.

As the muni bond market explodes for retail, institutional and international investors, experts at the FA Summit shared the latest updates.

Labeled vs. unlabeled muni bonds

One of the biggest challenges for investors is finding legitimate green or social muni options, as there may be labeling inconsistencies across the bond market.

Some are wary of "greenwashing," whereby issuers misrepresent their bonds' environmental impact for marketing purposes. However, there are also some muni bonds funding climate or social projects without the impact label.

"We see a lot of unlabeled impact [bonds] in the muni market, especially on the social side," said Michael Kashani, global head of ESG portfolio management at Goldman Sachs Asset Management and panelist at the FA Summit.

For example, there may be muni bonds funding the construction or expansion of K-12 schools in underserved communities without the "impact" label, he said.

Build America Mutual, the largest provider for external green bond verifications, has identified about 175 green U.S. municipal bonds worth about $2.5 billion, Levenstein said.

Over time, more social, green and sustainable bonds have aligned with one of the United Nations' 17 sustainable development goals, she said.

"I think the alignment provides further comfort to investors that they're buying legitimate green, social and sustainable bonds," said Levenstein. "And that's sort of where we see the market going in the next year."

Impact investing returns

While many impact-driven investors want to support green or social projects, portfolio returns are still the top concern, Kashani said.

But with approximately 50,000 municipal bond issuers and 1 million securities, there are endless ways to customize a client's portfolio based on individual preferences, he said.

"There's a lot of flexibility and variability, depending on how deep a client wants to go," Kashani said.

For example, some clients may prefer higher percentages of impact funds for specific sectors, which may affect returns. However, there are many options to bring "economic, environmental justice, transparency and equality" across their portfolio, without sacrificing their goals, said Kashani.

With current yields above Treasurys, muni bonds — which generally bypass federal levies on interest — have been a refuge for those worried about impending tax hikes from President Joe Biden.

Muni bonds, already known for relatively low default risk, scored a credit boost in 2021 as state and local governments received billions in federal stimulus money.

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JUN 30 2021