

# **Bond Case Briefs**

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## **Municipals & Climate Change Series: Drought & Extreme Temperatures.**

Municipal bond issuers are often linked to tangible, physical assets directly exposed to the effects of climate change. Over the long term, we believe municipalities will increasingly have to contend with the effects of this exposure, such as preparing for rising sea levels, managing constraints on local water supply, or rebuilding infrastructure after a hurricane or wildfire. This series will explore how various climate-related risks and policy responses could impact municipal issuers and describe our approach to assessing those risks.

In recent years, recurring drought conditions and rising temperatures have negatively affected large parts of the United States. According to the National Drought Mitigation Center, 76.4% of the western US was experiencing drought conditions at the end of June, with 38.1% under extreme drought.<sup>1</sup> Continually hot, dry conditions have constrained local water supply for municipal water and sewer utilities and could stress public power utilities. Here, we'll examine how these conditions can affect municipal utilities and how we approach these risks in our analysis.

### **Water and Sewer Utilities**

With drought conditions increasing in frequency and severity, water supplies for retail and wholesale providers are likely to remain constrained, particularly in the western US. Persistent drought has forced many utility providers to rely more on expensive imported water from state or regional sources rather than local sources. However, state and regional sources generally have many stakeholders and some have begun reducing annual allocations to retail providers, underscoring the importance of water rights, which determine priority access to water supply. Additionally, some municipalities have implemented voluntary or mandatory conservation measures to help combat supply challenges, potentially decreasing customer demand.

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