# Going green in munis — for the right reasons

Wealth Management

Since the first 'green' municipal bond deal was completed in 2013, issuance has increased slowly and they represent a small part of the municipal bond market. That being said with increasing demand for municipals in general and the ongoing interests on the part of investors in 'green' or socially responsible investing issuance should increase in coming years. In building diversified portfolios, investors should however look to balance their desire to invest responsibly versus building a diversified fixed income portfolio, especially since many municipal bond issues go to fund projects that benefit society in general such as infrastructure, education, and healthcare.

## What makes a bond green?

The cornerstone of a Green Bond is the use of its proceeds. The Green Bond Principles (GBP) recognize the following broad categories of Green Projects:

- Renewable Energy
- Energy Efficiency (including efficient buildings)
- Sustainable waste management
- Sustainable land use
- Biodiversity conservation
- Clean transportation
- Clean water and/or drinking water

These principles recommend that all designated Green Project categories provide clear environmental benefits that can be described, assessed, and quantified. The GBP was written to assist underwriters and issuers to move towards a standard disclosure that will facilitate transactions. RBC Capital Markets is one of the 25 investment banking firms that has signed onto the GBP.

## Munis, green with envy?

Since the World Bank issued the first green bonds in 2008, several supra-nationals, federal and local government agencies, commercial banks and private corporations have issued green bonds. In 2013 alone, green corporate bond issuance totalled $11.8 billion, up from $2 billion in the prior year. Issuance has increased further in 2014 with year-to-date issuance at approximately $20 billion.

Not to be outdone, the municipal bond market has recognized the opportunities with Green Bonds and in June 2013 the Commonwealth of Massachusetts issued the first muni green bond, selling $100 million green bonds as part of a $670 million of General Obligation bond issue. Since then there have been three other green muni issues: in June the New York State Environmental Facilities Corporation sold $213 million green bonds, in July the District of Columbia sold $450 million green bonds, and the State of California included $200 million of green bonds in its $2.1 billion issue in September. Based upon investor appetite in these recent deals there is much pent up demand which could likely foster increased issuance going forward.

## They are, after all, still an investment

From an investor standpoint, green bonds allow them to enjoy social and environmental returns, as well as financial returns. As a result, they are an attractive investment alternative as investors builds diversified financial portfolios.

It is important however for investors to evaluate green bonds, whether taxable or tax exempt, as they would any other investment from the standpoint of risks and returns, recognizing that being socially responsible doesn't necessarily guarantee superior returns. To date tax exempt Green Bond issuance has not been large enough to build a diversified Green Bond-only fund so performance is difficult to track. However, in a review of existing funds with a Green-bond component, Bond Buyer concluded the returns of these funds have lagged those of similar non-green funds. Furthermore, according to The Bond Buyer secondary market activity has been inconsistent with yields higher or lower than market benchmarks with light trading activity in some issues.

The bottom line is investing, even in bonds, entails risks and for many investors it is a balancing act to invest in a socially responsible manor while building a diversified investment portfolio. It is possible to do both, but in our opinion investors shouldn't let their desire to invest in green issues outweigh the need to make the appropriate investment decisions.



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