KEYNOTE INTERVIEW

Creating long-term value in early-stage renewables

The growing focus on the energy transition is highlighting the attractiveness of the renewable energy sector, says Daniel von Preyss of Impax Asset Management

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Q How has the attractiveness of the energy sector evolved as a result of the energy transition?

The new energy sector has been attractive since we first started investing in it 15 years ago. Although our journey in the renewables sector has evolved. In the early stages, there was more perceived technology risk, it was expensive, and investors relied on a tariff. Today, renewable energy has become mainstream. One can now take an industrial financial investor approach.

The key reason why renewables are more attractive today is that the efficiency and cost, predominantly for onshore wind and PV solar, are now very competitive when compared with conventional power generation sources. This is mainly due to the costs of construction and operations, which have come down significantly.

Our focus has traditionally been on Western European countries because they have clearer government policies towards green energy, less perceived political risks and a very competitive exit market. Germany and France are by far the largest markets and, if you are a major renewable energy player, those are the markets in which you want to be active. Each market has its own drivers and preferred technology. Further south in Europe, solar is more attractive. In the north, wind dominates.

When we first started investing in renewable energy assets, government support was a critical element in the economics. Although many countries in Europe continue to support new energy infrastructure build-out with feed-in-tariffs, these are now determined in an auction process and are increasingly in line with grid parity. The era of high and materially above-market, long-term, government-secured offtake agreements is over. This has removed perceived political and fiscal risk, which is good for long-term investors.

As an example, in France the auction feed-in-tariff for PV is about

€55 per MWh. The old tariffs in Spain and Italy were €200 per MWh or more while the price of power was nearer to €60 to €70 per MWh. Today renewable energy is a cost-competitive, efficient form of production that's also environmentally friendly. This, we believe, is the most notable change in the sector.

At the moment, we see plenty of interesting opportunities in the European market and don't see a strong need to expand outside the continent, which would also increase foreign exchange risk for our euro-denominated fund, unless we can find superior returns versus other European opportunities.

As single countries evolve, there will be times when they are more attractive and times when there may be fewer opportunities. Our strategy involves centralised know-how that can be easily transferred into each country where we see opportunities emerging, all while working with local partners or making local acquisitions.

Q What strategic challenges are facing investors today?

The challenge always lies in finding interesting projects. Given that we are looking to create capital gains, we need to find projects where we have an opportunity to come in early enough to create long-term value for our investors through our industrial expertise.

Otherwise, we are very comfortable with the sector, given our experience in it. We're not nervous about any one particular risk. It's more important to find the right projects at the right stage of development and then to minimise each project's development risk and maximise the potential to create value.

Q What are the main drivers for asset allocation in the renewables sector?

We are driven by wanting a diversified portfolio across countries in order to spread our risk more efficiently. If you are a premier European renewable energy fund you want to be in the

Buy, build and sell

Daniel von Preyss outlines the advantages of Impax's start-from-scratch strategy

Our investment philosophy is based on the belief that the transition to a sustainable economy provides attractive investment opportunities for our investors across the whole spectrum.

One of the drivers behind this strategy is that the energy transition provides an opportunity to invest in the fastest growing area of the energy market. We also focus on Europe, where there are key policies in place for a huge build-out of renewable energy projects and the replacement of conventional power stations by these new energy assets.

The EU has policies and targets regarding the transition, and in many countries these ambitions are continuing to develop further. The UK, for example, plans to go carbon-neutral and Germany plans to have, in the long term, 80 percent of its energy backed by renewable sources.

A value-add strategy presents interesting opportunities, and our 15 years of sector know-how related to securing projects and ushering them through late-stage development, construction and assembly of operating portfolios gives us a real advantage.

When we enter a project during the development or permitting stage, there are many ways to optimise it by adding efficiency, increasing output and improving the construction process, and thus improving the investment to create better value.

Once a portfolio is up and running, we sell it to long-term hold investors that are focused on operating assets. In other words, we are creating value for our investors by investing and growing a portfolio while creating environmental benefits.

largest markets, which are also the most attractive in terms of size and political stability. We also look to diversify across technologies and sectors, so that we are not exclusively in wind or solar or buying only one type of turbine – it is important to have different types of technology in our portfolio.

Going forward, we are looking at expanding into enabling infrastructure, which will increasingly be built up around renewable energy. Examples include storage or EV charging stations. As the sector becomes more mainstream, we expect many more opportunities for this enabling infrastructure.

Q What measures can investors take regarding environmental, social and governance factors when planning investments?

This is an important subject for us and is part of our core business across all funds. Sustainability has been embedded in our investment process for the past 20 years, and renewable energy itself is central to this strategy and aligned with our aim to facilitate a carbon-neutral economy. It is therefore relatively straightforward for us to provide impact reporting to our investors; several of them ask for ESG reporting.

The build-out of new facilities and projects goes through a very onerous permitting process. They must comply with environmental and social aspects because they are very much embedded in the local communities. We make our teams follow ESG-compliant policies. Our biggest measurement is the carbon savings, which is also quite key for our investors. Since 2013 the strategy has developed sites in 11 European countries with accumulative carbon avoidance of over 1 million tonnes.

In terms of displacing fossil fuel-fired generating capacity, we are building plants in countries where the policy is very much driven by a programme of replacing conventional power stations. Our impact is measurable and verified by an external auditor.

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Q What risk management strategies do you have in place?

A key risk within our strategy is during late-stage development, and there are various ways to manage this. First, before we secure projects or acquire companies, we conduct due diligence to make sure we are comfortable with what we are buying. We have a very clear strategy and mitigation programme in place for the risk we are undertaking and our ability to manage it.

Second, when we acquire a project, we structure the investment carefully to ensure we make payments in line with key milestones such as when portfolio assets are de-risked.

In addition, we like to acquire portfolios of projects so that we diversify project risk. That way, we are not putting all our eggs in one basket. Even if one project might underperform, we have factored this in at an early stage of the investment decision.

In terms of construction risk, we look for good-quality equipment and counterparties – we're not necessarily focused on the cheapest, but on the most economical option that allows us to maintain quality. When appointing contractors, we aim to pass through potential risk such as delays to construction. This means that we have an embedded insurance within our construction contracts.

Overall, we're seeking to build new infrastructure and not just taking part in a cost-of-capital shoot-out for trophy assets. We're creating value for our investors by taking advantage of the new build opportunities. We strongly believe there is a gap in the market. There's a lot of money for long-term assets, and it is a very competitive market. But we feel there is not enough capital or investors that understand late-stage development and construction risks, and at Impax we are filling this gap. ■

Daniel von Preyss is head of private equity infrastructure, Europe, at Impax Asset Management