KEYNOTE INTERVIEW

Helping the energy transition entrepreneurs

RGreen's Nicolas Rochon, Cédric Lacaze and Jacques Çikurel consider the importance of entrepreneurs to the energy transition

Focusing on small- and medium-sized businesses at the crucial inflexion point between start-up and scale-up is the key to accelerating Europe's energy transition, believe RGreen Invest's founder Nicolas Rochon, managing partner Cédric Lacaze and senior investment director Jacques Çikurel. Unlike traditional energy, the space is dominated by small entrepreneurs, and those parties are of critical importance to drive a successful transition.

The French investment management company originally invested tickets in the €20 million-€30 million range, but as investors have flocked to the asset class, the firm's investment size has also grown; it is now around €75 million-€100 million. The three executives consider how the space has changed, where it is heading, and why it is the smaller players who will be most important in that process.

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Q Why are investors flocking to transition assets?

Cédric Lacaze: What makes the energy transition proposition attractive for investors is the natural protection the asset class offers against inflation. Interest rates have gone up, driving discount rates higher and negatively impacting the valuation of the assets.

At the same time, the price of electricity has also increased, driving revenues higher, which offsets the negative impact of rising interest rates and protects the value of the assets. Transition assets thus have a natural hedge against inflation, particularly in countries dependent on fossil fuels, that is not true for other infrastructure assets.

When interest rates go down, as they are likely to do in the future, discount rates will follow, providing an uplift to the current valuations. This means investors deploying capital today would be positioning well for realising the upside in a resilient asset class.

What are the main sectors that are attractive to investors at present?

JC: We think there are three key pillars: renewables, electrification and energy efficiency. Energy efficiency is more in the value-add space and therefore not our top priority, although we could get involved in an opportunistic way.

Renewables is the most mature of the three pillars and whilst there are significant opportunities in areas such as solar, wind and hydro power, some areas of innovation may offer the best future returns. We are also looking at areas such as biogas and geothermal and have been involved in one project at Disneyland Paris which is currently small but indicates the potential of the subsector.

Electrification is a less mature area than renewables but also somewhere where innovation is important. We see a lot of activity and opportunities in electric vehicle charging and battery storage infrastructure. Storage is clearly going to be very important as we move into an environment where we need to fully capture the potential of renewables.

NR: That innovation is crucial. You are not going to make significant money by investing only in the vanilla projects. We are constantly looking at areas of innovation such as what is happening in the agri solar area in Europe, where you are combining energy generation with other benefits for long-term sustainability.

Nicolas Rochon: Infrastructure investors are always looking for assets that are resilient to the boom-and-bust cycle.

But what is most exciting now is the drivers of demand energy growth.

Jacques Çikurel: The primary driver is the electrification of every part of the global economy. This is creating a massive increase in electricity demand, which will need to be reflected by a significant expansion of energy generation assets. Investment in fossil fuels will remain limited going forward, so Europe will need to deploy significant renewable energies to meet this demand, as well as technologies to manage the intermittency, including energy storage.

Today, electricity demand is particularly being driven by two trends: the electrification of transportation supported by regulators, and the impact of digitalisation, which is leading to demand growth in data centres, which by their nature are energy hungry.

NR: We really need to be developing a lot of renewable energy projects now to address what is essentially an energy emergency. It should also be added that certain technologies such as hydrogen and nuclear are simply not solutions for today. They will play no role before the mid-2030s.

So, is the investment opportunity simply about demand growth?

NR: Not at all; it is also about what is happening with capex. The key to energy transition success is producing energy at the cheapest possible cost. Capex deflation is now accelerating thanks to geopolitical events. The US actions to restrict Chinese imports into their economy have created significant opportunities here in Europe, where there is frankly oversupply of those Chinese manufactured components, particularly solar PV modules.

This means energy transition investors have that most precious commodity in investing: clear visibility of returns for at least the next 24 months.

How about regulation to encourage investment?

NR: We have moved beyond relying on them. Yes, subsidies were important to get renewables off the ground, but now they are truly profitable in their own right.

Going forwards, I think what we need from regulators is not cash, but rather simplification. Simplification in the development process, less regulation, less administration.

CL: I would go so far as saying that there is an essential contradiction between a commitment to climate change and an addiction to bureaucracy. Regulators must accept this.

NR: One thing is true: European regulators are certainly optimistic. Their targets imply that in the next seven years we will achieve what it has taken us 40 years to achieve so far.

Europe has a massive challenge when it comes to adding renewable energy to its grid, but the reality is that the grid is different in different markets. Each country must make an effort, and the ongoing integration of the European energy markets needs to speed up.

Q Which are the more interesting countries from an investment perspective?

JC: Some have made very significant investments in renewables, but this means that the opportunity set is somewhat mature for them. Spain has considerable PV capacity, and the Nordics have a lot of hydropower driving lower captured prices.

The more interesting opportunities are in those markets which are currently dominated by fossil fuels. So, Italy is one country that stands out. We are very interested in opportunities there, including in biomethane. We partner with developers who can make a successful transition to an independent power producer (IPP), that is where the excitement is.

NR: The key to that is timing. It is crucial that you invest at the correct inflexion point, just before a business takes off. You have to catch them when they are ready to scale up and capture economies of scale.

CL: There is a recognisable life cycle to an IPP company. Typically, it will be in its development stage for the first five years of its existence, and the valuation of the company might be in the range of €50 million-€100 million while it develops and matures its assets, and perhaps builds a number of these that reach ready-to-build stage.

At this initial stage, the value creation multiples are very high, but the capital deployed is fairly limited. It is at the end of this stage that we enter the scene, so that we may benefit from the second stage of growth which requires much more equity and debt capital.

That second stage is when the company makes its transition from being a start-up developer to a fully-fledged IPP. A lot can happen quickly with the availability of capital, propelling these businesses towards the billion-euro valuation point.

As they come to the third stage, where most growth has happened, then this is the point at which a company might be more attractive to core infrastructure investors who prefer a lower risk profile. This would be the stage where we would seek to move on.

For us, the second stage is the sweet spot, with an attractive trade-off between risk and reward.

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>
> **NICOLAS ROCHON**

Q What are the prospects for the energy transition?

NR: The potential in the energy transition space is huge. There is a lot of value to be created and a lot of growth to be financed.

We currently have more than €2 billion under management, and we expect to invest some €10 billion in the next 10 years. This is the scale of what we are talking about.

But to get there will require different skills. They are certainly different to traditional energy investment. Successful investors will need to have the capability to manage core energy production, but also to negotiate the best price for that energy.

It used to be all about producing, whereas in the future it is going to be much more about producing, managing and optimising. The key to creating value in the energy transition will be to successfully blend all of these elements.

I also think success will only come for those who are genuinely mission-driven and have a real understanding of the underlying principles. We strongly believe what we are doing is vital to the success of energy transition in Europe. It can only come by giving entrepreneurs that helping hand necessary to achieve scale. ■