

# KEYNOTE INTERVIEW

## Adjusting to a post-subsidy market



*The post-subsidy world is impacting leverage availability, future price projections and returns. But exciting new business models are also emerging, says RGREEN INVEST's founder and managing partner **Nicolas Rochon***

**Q Where are you seeing the most attractive investment opportunities currently, in terms of clean energy generation in Europe?**

We believe that the most interesting opportunities in terms of risk and return, right now, can be found in eastern Europe. Poland is an attractive market with very good wind conditions, although we think returns will start to come down there in the next six months or so because of increasing competition.

We also envisage opportunities opening up in markets such as Hungary and Romania, which are emerging as new strongholds in renewable energy generation. At the same time, we continue to see great opportunities in countries like Italy, where we have been operating for a very long time.

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Interesting solar projects, in particular, are being developed in that market with revenues that are secured, not with feed-in tariffs, but through sales to market or through private power purchase agreements.

**Q To what extent have the parameters of investment in energy transition extended beyond these traditional forms of energy generation?**

Of course, you have solar and wind and those remain very important for supporting global energy transition, but the reality is that returns in those sectors are rapidly decreasing. We believe

the next big opportunity involves innovative business models. Combining solar energy generation with agriculture, for example. There are dedicated auctions taking place for these types of initiatives and those have the potential to offer far more attractive returns than pure wind or solar projects.

There are also emerging opportunities around energy efficiency and new developments in hydrogen that look attractive. And, of course, energy storage has a great potential going forward.

In short, we see mature sectors such as pure solar or wind being disrupted by innovative hybrid business models that can generate higher returns. In addition, we need to constantly pay attention to the emergence of new energy efficiency technologies that could well become tomorrow's blockbusters.

**Q What opportunities, and challenges, has a shift from feed-in subsidies to more merchant risk created for investors in this sector?**

The first challenge involves the gearing of projects. Historically, long-term senior debt has represented 80-90 percent of the capital structure for renewables projects. That has now fallen to close to 50 percent. This makes sense from the lenders' perspective. There is less visibility around future cashflows, so lenders want to reduce their exposure to any possible fluctuations in price, even though the volume is secured.

The challenge for developers and operators is this means they need to invest more equity than before. Even though the cost of installing solar and wind has decreased significantly, the reduction in available gearing can still prove difficult and this is an area where we have been able to provide solutions that don't dilute ownership of assets.

Another challenge associated with the shift to a merchant risk model involves production and price projections which have become significantly more difficult to predict than before.

In Spain, for example, there is a massive solar boom going on, with lots of projects in the pipeline representing huge volumes of gigawatts which will have a negative pricing impact when they are ready to connect to the grid. All these plants will be producing electricity at the same time, between 9am and 6pm when the sun is shining and that will inevitably push prices down. It is vital that you take these projections into account when putting together a business plan where pricing is not secured for the lifetime of the project. Of course, you can secure a corporate PPA for five or 10 years, but this does not match the level of price security we once had.

**Q Bearing in mind those challenges, how would you describe competitive dynamics in the energy transition markets where you are operating?**

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It depends on what you are looking for. Big infrastructure funds looking to put large tickets to work will all end up competing on the same projects, because there are limited opportunities of that scale in Europe right now. We don't compete in that end of the market. We make smaller investments in areas where we face lower competition.

We are very cautious around bubbles that are emerging in some areas. Prices for ready-to-build solar projects in Spain, as I mentioned, are soaring, while the future price of electricity is falling, therefore we do not believe returns in that sector are going to prove very attractive. We prefer to operate in countries where we have a competitive edge, such as Italy and Poland or to invest at the development stage to avoid competition all together.

**Q What are the risk/reward dynamics of investing at the development stage?**

This is a new opportunity for us. In the past, taking development risk was difficult because of the cost of producing

renewable energy. Now that renewables are competitive, it is possible to take more development risk. It is no longer binary. It isn't the case that you either secure a feed-in tariff or you don't – in which case you have to wait however many years to try again. Now, you know you always have the option of selling the electricity to the market or via a corporate PPA.

In addition, the cost of development is around €30,000 to €50,000 per MW. That can be three to four times less than the cost per MW at a ready-to-build stage. We see that as a key means of protecting ourselves from competition and price inflation. As a result, we have decided to dedicate around 10 percent of our fourth fund to this type of pure development risk, compared to just 2 to 5 percent for predecessor funds.

**Q How would you describe LP appetite for energy transition?**

Appetite is certainly growing, not only for renewables but for everything related to reducing CO2 emissions. Almost everyone understands that the world is facing a major problem, and people want to be a part of providing a solution. Renewables obviously have a major role to play in that, but there are other ways to cut emissions, too.

Again, that is why we have evolved our strategy with our latest fund. Around 70 percent will be deployed into renewable generation projects, but 30 percent will also be deployed into other types of technology addressing energy efficiency and climate change resilience. There is a great deal of appetite from LPs in these areas.

I would add, however, that despite a growing interest in energy transition investments, LPs are also showing concern around the amount of capital flowing into these asset classes and the impact that will have on returns. There has been a massive proliferation in funds dedicated to infrastructure and renewables, in particular, and that has created some caution amongst investors.

### A symbiotic approach

#### New models mean solar and agriculture can work hand-in-hand, says RGREEN INVEST's partner and investment director Olivier Guillaume

Europe is facing a significant challenge. A clear desire to increase solar capacity is limited by land availability. This conundrum is leading to some innovative solutions designed to mix energy production and agriculture in the same location. But, to date, none of the existing technologies have yet succeeded in producing solar energy without reducing agricultural yields. Solutions involving greenhouses for example have not proven to be efficient for supporting crop growth; the reason being that if crops need more and more shade over the year, they also need direct sun over specific periods that fixed or full tracking PV cannot provide.

RGREEN INVEST is now working with a pioneer company in France that has developed, over the last decade, a proven solution that uses agronomic tracking technology to manage the solar panels and optimise the solar energy received by the plants growing below. It is an entirely novel approach. The owner of the solar panels agrees to lose between 10 and 20 percent of energy production, depending on crop type and location of the project, in



order to increase the production of the crops. This technology is ideally placed to operate in countries that are short of space, inducing choices between the use of land for agricultural production on one side and for clean energy production on the other – both of which are obviously hugely important, but increasingly conflictual.

Most of all, this solution is critical in terms of adaptation to climate change. This is an important evolution when it comes to energy transition. Take the south of France, Spain and Italy – all areas where temperatures are rising. Certain agricultural practices – wine production, for example – are increasingly challenged by the more extreme climate conditions. Real-time agronomic tracking of solar panels above vineyards can protect grapes from the worst excesses of climate change and climate hazards. In this way, this technology can be used to produce electricity and provide climate change resilience for farmers at the same time. We see it as a hugely positive development, and this is exactly the type of area where we are increasingly looking to invest.

#### **Q** What is your approach to asset management in the energy transition space and to environmental, social and governance in particular?

It is easy to think that just because you are invested in renewable energy you have ticked the environmental box.

In reality, there are real challenges involved in ensuring the best possible environmental outcome.

You need to think carefully about your EPC contractors and make sure you are selecting the right manufacturers for solar panels. Making sure you are working with the right suppliers is incredibly important when it comes to ESG best practice. We are convinced about that, and we always work hard to reinforce our ESG policy throughout the supply chain.

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#### **Q** What do you believe the future holds for the energy transition space and what do you see as infrastructure investors' role within it?

We are convinced that the next industrial revolution will be centred around energy.

The last 10 years have only seen the very beginning of the energy transition story, with the growth of solar and wind initiatives. Going forward, those sources of alternative energy will be critical to all sectors and markets.

The agricultural sector, the mobility sector, the construction industry, are all going to incorporate new energy solutions in their business models.

The future will undoubtedly be fuelled by green energy. ■