Shades of green

In Europe and the US, the growth of renewables, buoyed by public opinion, has shifted the energy equation. **Dean Kennedy**, Deutsche Bank's London-based Global Transaction Banking product manager, and **Brent Canada**, the bank's New York-based head of infrastructure and energy debt origination, share their views from both sides of the pond

Q What trends are you seeing in the renewables space?

DK: The investor landscape in Europe continues to change. We have acted as the agent and conduit between the borrower and bank investors in the typical syndicated loan form for many years. It has only been in the last three years that we have seen a significant shift. We now work more and more with institutional investors of infrastructure debt, initially with the likes of PPP road projects and social infrastructure. Now we are seeing appetite for offshore wind and solar PV.

This focus from institutional investment obviously leads us to long-term support for pension funds and insurances companies who need to match their long-term liabilities. That is the trend in Europe. From the relatively safe option of availability-based road projects to the more risky offshore wind parks, this is a trend we had expected to happen, but not as potently or as quickly as it did.

BC: Everybody is talking about storage. If you asked six months ago, people would say they are interested in storage but it will take a while to develop. When you talk to those same people today, they are actively looking for opportunities.

We are keenly focused on storage and I think we are more bullish than the general sentiment around the development timeline. Most people we speak with view storage growth over a five-year horizon, whereas we expect this asset class to be a significant part of our 2019 budget.

Q Offshore wind has seen a surge in activity recently. What is driving this sector, and what can we expect to see moving forward?

DK: Our focus in this space has been in the UK and Germany with an eye on the Netherlands and Belgium. We still see bank financing leading the charge here. From a greenfield perspective, pricing has been driven lower and lower. That has led to some fierce competition from banks who want to have skin in the game when it comes to long-term commitments. The prospect of zero-subsidy bids widening, as we saw recently in Germany, which in the past has not been really suited to renewable energy.

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With the main winners of the UK's latest CfD auctions being offshore wind projects, and 1GW awarded in Germany will lead to multiple opportunities. The interesting thing, perhaps, is also the technology advances in the space that we are seeing. There is potential for the larger, 10MW turbine blades that we will be seeing shortly, and a lot of focus on floating offshore wind, which would allow these wind parks to be further from shore, lessening their environmental impacts. We expect more opportunity as technology advances continues and investor appetite diversifies.

BC: I am not super bullish on offshore wind in the US. Europe has a much longer history of offshore oil drilling and it has substantial infrastructure which has been built up over the years to support it. Because of that, when it decided to develop offshore wind, it already had a lot of the necessary infrastructure in place to develop these projects. Because of this, the capex required to set up wind farms in Europe is much lower than in the Atlantic coast of the US, where you just do not have that same infrastructure. The projects that you have seen in the US are less about the US being the optimal place to have offshore wind and more about European developers running out of coastline in Europe and looking at the US as the next spot to develop.

Q How are green project bonds, and now green loans, playing increasing roles in the sector?

DK: Global green bond issuance volumes are set to exceed $130 billion in 2017. With increased political will, developing frameworks and more focus on the Green Bond Principles, there is a lot of discussion on whether could support more stringent requirements for issuers around transparency, disclosure and reporting in terms of what qualifies as a green bond.

A good example of the categorisation shift is the refinancing of an offshore wind project in Germany. That was a multi-source refinancing from construction on the bank debt to bonds being issued in Europe and in the US. That financing, which was categorised as being a project bond, was labelled as a green bond. In that case, it was clear that this financing was going towards the operation of a green asset.

Most recently, Anglian Water, was effectively the first UK utility to be listed in the green bond segment of the London Stock Exchange. It shows the diversity in what the GBP is trying to capture, and the focus of issuers in the market looking to issue green bonds and meet with the GBP criteria around ESG.

Q Which country-level trends are most compelling?

DK: From my perspective, the most interesting is southern Europe, particularly Italy. In the debt financing space, we have seen a surge in activity, where in the past it was nearly impossible for unlisted companies to issue debt. With an improved macroeconomic environment, a more stable regulatory framework and some changes in tax regimes, there's increased appetite for Italian wind and solar assets. We have seen a move to " mini-bond" financing for renewables, which in the past was only available to large issuers and listed companies and banks.

Since those changes and those rules have been put into place, there have been a number of renewable project bonds, which is a key focus for our business and the bank as a capital markets player. Those changes, which allow investment into these types of assets, are going to lead to more private investment in the renewable space. And of course there have been subsidy auctions happening across Europe, including in Italy and Spain. In Italy, the government said that it is looking to invest up to about €9 billion over a 20-year period and there continues to be a positive focus in that region around the renewables share of the energy market.

Q Will uncertainty from a policy standpoint hinder the renewable market in the US?

BC: I believe the economics of renewable power in the United States are so overwhelming that while you may have some blips along the road, whether from policy or public sentiment, the market is going to continue. Coal-fired generation is likely to go away. Nuclear generation is likely to go away. Gas fired generation, will have its brief moment because of shale, but you will likely see that being chipped away pretty quickly too. Renewable power is the one source of generation that I think you can bank on for the long term.

Q How has the way clean energy projects are financed changed?

DK: In some cases it has changed and in others it has not. Bank debt, which was dominant in financing projects, continues. There is a long list of banks that are vying for offshore wind projects, driving down pricing. As mentioned, we have seen an appetite from institutional investors to be involved in offshore wind, not in the form of true greenfield risk but as part of an acquisition, and in some cases a construction wrap.

In solar, there is a clear shift towards institutional investment with growing appetite and understanding of the asset class leading to innovative structures still involving banks. In evidence of that, Deutsche Bank itself will likely have placed more than €700m of Spanish solar bonds by the end of this year. That trend is set to continue in the known asset classes such as wind and solar, but there is a need to build the merchant market, with institutions taking a controlled merchant risk. Biomass continues to be interesting, as we are now seeing some of the bigger institutional investors come in and want to commit, in the long term, to such projects, particularly in the UK where we are now supporting a number of projects.

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Q For many investors in renewables, making a positive impact on the world is an important component of their investments. How is that balanced against the need to maximise financial performance?

BC: When you speak with renewable power developers, and hear how they present themselves, there is definitely a very 'green', clean message that is put out there. But when you speak with the providers of capital to these institutions, the conversation is almost entirely an economic decision. You are not seeing hedge funds and private equity funds and other pools of private capital pouring money into renewables simply because they want to be 'green'. These are asset classes and projects that make sense on a standalone basis.

From a bank standpoint, we are certainly cognisant of the positive impact of participating in these markets, and that is a key element of why we are so focused on this sector. That being said, renewable projects are an efficient way for us to deploy capital from a pure economic standpoint. ■

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