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Green growth gathers pace

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Getting institutional investors to take risks is never easy, and convincing them of the charms of green investing has proved a challenge. But some recent large-scale renewable energy and environmental deals have shed light on a sector previously in the shadow of traditional oil and gas.

The lack of track records, shifting regulation, and competition with low-cost technologies coming out of Asia may continue to deter a portion of institutional capital, even if a maturing sector is beginning to offer a compelling infrastructure investment play.

The biggest green private equity funds now match the fund sizes of counterparts in many sectors. But while once the principal route for many investors seeking to access the sector, private equity funds are no longer the only option.

Warren Buffett's recent solar bond, carried out through power generation developer MidAmerican Energy, was more than $400m oversubscribed, and is one of the clearest examples of investor appetite in this area, as well as the willingness to explore new strategies and industries.

Out of the shadows

Dima Rifai, managing partner at financial services firm Paradigm Change Capital Partners and recently appointed adviser to the UK's Green investment Bank, says, "Private equity has been the big driver to date for the major investors, but as their awareness goes up, so too do access options. Now institutionals are participating in bonds, investing directly and co-investing alongside funds."

She adds, "Initially, pension funds, sovereign wealth funds, and family offices were all beginning from a pretty uneducated place. They are doing constant relative value analysis, and this industry has to stack up."

European reinsurer Munich Re recently committed to a €2.5bn spend in the green space, principally through direct investments, which have already included investments in the German power grid and solar power plants in Italy and Spain.

And one company that has already taken advantage of direct institutional participation is energy developer Alterra Power. Large investors are becoming more comfortable dealing directly with developers, says Anders Kruus, vice-president of corporate relations at the Toronto Stock Exchange-listed business. Its subsidiary, geothermal developer HS Orka, recently secured additional capital from Jarðvarmi, a group of Icelandic pension funds. European investors are often more forthcoming than US groups, he says.

"There is definitely a broad acceptance and openness to renewable energy investment – at least publically listed investments – in Europe. European institutional renewable energy investors tend to have substantial pools of money with long-term horizons, while many US investors face constraints from tighter mandates and benchmark tracking limits."

Success stories

For those committed to the private equity route, renewable energy fund managers face the challenge of proving the investment strategy is not only attractive in its own right, but also that it stacks up against more mainstream energy and infrastructure sectors.

Roger Ammoun, director of customised fund investment group at Credit Suisse Alternative Investments, says, "Because of what has happened in the history of the sector so far, there is still a stigma associated with the lack of returns in the asset class. However, there are very good success stories as well."

The type of institutions committing capital, both directly and through funds, has also altered, he says. "The mix of investors has changed. Between 2006 and 2008, institutional investors were willing to put a cheque on the table. Now it is strategic investors who are still there. Private wealth capital is looking at this from a social perspective or from a high-risk, high-reward opportunity.

"The challenge with institutional investors – and here I am thinking funds or large endowments – is to convince them the strategy makes sense."

And for private equity firms looking to raise a fund in the space, family offices may prove a useful source of capital, according to Bill Rogers, managing director at green private equity heavyweight Hudson Clean Energy Partners. "Family offices are pretty knowledgeable as they are entrepreneurial, and often based on wealth drawn from a previous entrepreneurial venture," he says.

The relatively small size of many renewable energy or environmental developments compared to larger infrastructure projects also appeals to this investor group.

Erich Becker, infrastructure partner at investment firm Zouk Capital, adds, "What's important to family offices is size. As they are often limited in size for each investment, it can often be easier to become involved with a 5MW wind project than a road project.

"They are very fast to commit and they are often very keen to take a hands-on approach. As such, you need to decide whether they want to do direct, co-invest, or whether they are happy to hand over control of the investment to a private equity fund manager." ■

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