

KEYNOTE INTERVIEW

Striking a sustainable balance



*To be successful, investments in the energy transition must balance support for emerging technologies and asset-heavy businesses, according to Nuveen's **Joost Bergsma**, **Biff Ourso** and **Don Dimitrievich***

Energy transition investments have evolved over a number of years, impacted by technological, market and regulatory developments. In light of this, managers have seen opportunities come and go, accepting that a one-size-fits-all approach is no longer fit for purpose.

Joost Bergsma, global head of clean energy for Nuveen Infrastructure, Biff Ourso, the company's global head of infrastructure, and Don Dimitrievich, senior managing director and portfolio manager of energy infrastructure credit, outline the importance of remaining open-minded and flexible when crafting investment strategies. This is

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especially true in the fast-moving energy transition space.

Q How is the macroeconomic environment impacting the investment climate around the energy transition?

Biff Ourso: From an investor perspective, we don't believe the macroeconomic climate has diminished the appetite to support energy transition goals. We recently completed a global

survey of more than 800 institutional investors and found that over half believe their allocations are positively impacting the progress of the energy transition.

What is more, seven out of 10 are going above and beyond any regulatory requirements in this area. Investment return is the most important driver here, followed by portfolio risk management.

Joost Bergsma: Over the last 18 months there has undoubtedly been a series of pluses and minuses from an equity perspective. Of course, the sector is not immune to rising interest

rates, and this has caught out some investors. Many energy transition projects, particularly in offshore wind, for example, are long-dated and so rises in interest rates can substantially alter their economic viability.

Supply chain issues also cannot be ignored. On the positive side, power prices are quite a bit higher than they were two years ago. Geopolitical uncertainty has also resulted in energy independence driving a lot of investment.

Don Dimitrievich: There are certainly headwinds, like the aforementioned issues around the cost of capital and supply chain disruption, as well as political uncertainty, with around 40 percent of the global population set for elections over the next 12 months. However, there are offsets to these headwinds.

Infrastructure is seen as a defensive asset class, so a lot of infrastructure assets' attributes, such as contracted cashflows with quality counterparties, are particularly attractive in a more volatile environment. While some projects may have become less profitable due to increased cost of capital or inflationary pressures, these sub-tier projects are not the ones we are investing in.

Q What is the importance of striking a balance between existing proven technologies and newer ones in energy transition investment?

JB: For the first 10 or 15 years after the energy transition agenda came to the fore, investment focused on power generation because this was the most carbon-intensive industry. Now, when it comes to raw power generation, there are three technologies really taking the lead in terms of cost-competitiveness: solar PV, offshore wind and onshore wind.

From a power generation perspective, most capital is set to flow here. Having said this, where investment in



Q Are there any geographic differences in terms of how different markets are treating the energy transition?

Joost Bergsma: The energy transition is a global movement, which makes regional differences extremely interesting. In parts of Asia-Pacific, for example, we see nuances across South Korea, Japan and Australia. Despite the global dynamics, this is a heavily regulated sector, so you still need boots on the ground and local know-how to capture the best opportunities.

Don Dimitrievich: There has been a politicisation of the energy transition, especially with elections on the horizon. What is interesting is that many traditionally “red” US states, such as Texas, remain active in the energy transition, with wind accounting for 25 percent of electricity generation, which highlights the breadth of the decarbonisation movement.

The other geographical distinction we are seeing concerns whether natural gas has a role to play in the energy transition. In the US, this is still viewed as part of the solution, at least until renewables can be used for the entire energy supply.

newer technologies is needed, governments could do more to make projects more effective and connections between assets more seamless.

The way investments are structured has also changed. It is not necessarily the case that each investment needs to be innovative per se, but we are likely to see more innovation in the revenue offtake side.

When we started investing in power generation, we didn't need to worry about revenue offtake at all, receiving a fixed, inflation-linked price from the

government. This paradigm has completely changed.

Today, when we invest in an energy transition project, we have to structure the offtake ourselves. Although we still pay a lot of attention to the quality of the assets, we now also focus on structuring the revenue side.

DD: If you look at the evolution of sustainable power generation, this decade will see the proliferation of battery storage to resolve some of the potential grid stability and intermittency issues

surrounding renewables. We see a lot of opportunity in this area as these technologies develop further and the cost curve comes down.

Another area with a lot of potential is energy efficiency, where you can implement AI and more energy-efficient equipment to reduce consumption.

The scale of the energy transition opportunity and the overall expansion of the addressable market require significant capital. From a credit perspective, debt will typically serve 60-80 percent of the cap stack – that represents a significant amount of capital and investment opportunity in the energy transition.

As different asset classes emerge, they are going to require significant credit capital and equity capital. So, it is not that new classes of debt will emerge, but that we will see more nuanced sources of capital for these types of projects.

As markets evolve, we will see different ways to fund projects, including some innovative applications in credit and equity. Then, if you also consider government programmes, like the Inflation Reduction Act in the US, we are seeing new, hybrid tax equity structures. So, there are certainly new investment applications being applied to traditional project development approaches.

Q What are the most interesting investment opportunities?

DD: One of the investment themes we are witnessing is the onshoring of the infrastructure supply chain. There are geopolitical and energy security considerations here, so we have seen the political wind change to recognise the importance of a domestically sourced energy supply chain.

As such, there are a number of projects we are looking at that are being driven both by government incentives from the Inflation Reduction Act and the belief that you need to onshore your supply chain. From a credit lens perspective, these projects have all the

classic attributes of an infrastructure asset to make them attractive. Developers are also looking for locally sourced equipment to help them moderate some of the supply chain issues.

JB: There is still ample appetite on both the equity and the debt side to invest in the energy transition. What is changing is that investors in the relevant technologies are now more sophisticated.

There is over a decade of track record for many of these assets. In the past, we may have had a one-size-fits-all approach, but today investors are trying to bifurcate and we also see an appetite for open-ended formats.

Q How important are regulatory frameworks to the energy transition?

JB: Further government input is still needed in this sector. Although many governments have been successful in driving down costs, more support is needed around newer technologies, like battery storage. This also has to be quicker, as infrastructure investors need to see predictable revenue.

Governments are still very slow at developing solar and wind projects in some countries. And the interconnection of assets remains an issue, especially in Europe. Governments are laggards here.

“We are likely to see more innovation in the revenue offtake side”

JOOST BERGSMMA

BO: From a North American perspective, it is well known that we still need more investment in the grid and there remains an incredibly long permitting process for transmission lines. This is something where government action could lead to greater project efficiency.

Secondly, across the world in 2024 we expect heightened political risk. So, even where there is substantial government support and guidance, challenges remain that require specialised understanding and sector knowledge to navigate.

Q How do you see the energy transition developing?

BO: Our core focus is helping our clients invest across the capital spectrum by delivering attractive risk-adjusted returns. Over the next three years, we see an opportunity to invest billions in this theme. We think it takes specialised expertise to do this effectively as the energy transition is a fast-evolving theme.

To invest successfully in this area, you need synergy among your teams. At scale we can offer specialised teams of engineers in various technologies and people steeped in decades of experience in this sector. That combination of expertise, history, deal-making and capital-stack understanding sets us apart for our clients.

DD: You can't be a tourist in this space. Our ability to leverage internal knowledge here is incredibly important.

As the addressable market continues to expand, incremental capital will be required, and we are at the forefront of discovering what type of capital will be needed.

While newer players can sometimes miss things, our longevity means we have seen the energy transition evolve over a number of years. We look forward to playing a leading role in its continued evolution – in terms of technologies, strategies and meeting our client goals. ■