Renewables in the age of Trump

With a president who has promised to revive the coal industry and leave the Paris Agreement, how will US clean energy infrastructure continue to grow as an institutional investor oportunity? Quinbrook co-founder **David Scaysbrook** outlines possible scenarios

IT IS OFTEN said that the best-laid plans have unintended consequences. So it seems to be with President Donald Trump's scuppering of the EPA's Clean Power Plan and withdrawal from the Paris Agreement.

The plethora of announcements of increased pledges and commitments to renewable energy in the US since President Trump's energy and climate policy reversals have stimulated what looks set to be an unprecedented build-out of new renewables infrastructure. The tangible job creation and regional investment stimulus that comes with this may be overcoming Trump's populist politics via the 'hip pocket' – more jobs and improved energy affordability.

These bolder commitments have come from US states, cities, local municipalities and, most importantly, from the largest corporations in the US economy and the leading US institutional investors.

To convey a sense of this wellspring of resistance to the president's policies since his election, consider these recent events:

- California (the world's fifth-largest economy) announced plans to legislate SB100, a proposal to increase the state's renewable energy goal to 100 percent of electricity generation by 2045 and 60 percent by 2030. California legislators also extended the state's carbon emissions cap-and-trade programme through 2030;
- The governors of the nine-state Regional Greenhouse Gas Initiative committed to even more ambitious plans to reduce carbon emissions by at least 30 percent below their 2020 cap by 2030;

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- Sixty-two percent of Exxon Mobil's shareholders voted in May to compel the company to assess and disclose how it is preparing its business for the transition to a low-carbon future. Resisted by senior management, the fossil energy behemoth's owners (led by institutional investors with $5 trillion of combined assets under management) won an unprecedented and unexpected victory;
- In June, a bipartisan group of mayors from more than 250 US cities passed the "Clean Energy Resolution", which committed their cities to run entirely on renewables by 2035 in a symbolic resolution aimed squarely at Trump's position on energy and climate issues. Ironically, the resolution was proposed by mayors from the key Republican states of South Carolina, Texas, Utah and Iowa;
- And finally, 43 percent of the US *Fortune 500* companies have adopted renewable energy and sustainability targets, with at least 22 of them committed to powering all of their operations with renewable energy, such as Wal-Mart, General Motors, Apple and Google.

While renewables investment to date has been driven by state Renewable Portfolio Standards, these recent commitments are coming from a broad cross-section of the country. Not surprisingly, staunch Democrat states such as California have increased their renewables commitments aggressively in response to President Trump. But 'less obvious' states are also getting in on the act, such as Nevada, Minnesota and Oklahoma, many of which are 'die-hard' Republican.

The push for more renewables investment seems to be finally all about the bottom line – jobs and cost.

AGEING FLEET

President Trump cannot change the fact that the average age of the US coal-fired power station fleet is 39 years and that they are more polluting, increasingly less efficient and, most importantly, more expensive to run than the latest generation of

renewables technology led by wind and solar.

Renewable costs have fallen more than 60 percent on average over recent years to a point where renewable power is being sold long term in some states at less than 2 cents per kilowatt/hour. For the first time, we are seeing coal plants becoming uncompetitive against new renewables on a cash-cost basis. Institutional investors know that, which is one of the reasons so few – if any – of them are prepared to invest in new coal-fired power infrastructure in the US today.

So when it comes to the all-important issue of cost competitiveness, renewables are now winning. They are winning in the contribution to GDP stakes, growth in new job opportunities and economic stimulus to both rural and urban communities that are hosting new renewable projects. Those facts get politicians elected and fired so that is the real game-changer, no matter what your political persuasion – especially in the US.

But simple cost advantage doesn't tell the whole story because this isn't an apples-to-apples competition we are talking about. The energy debate in the UK, Australia and many US states has recently shifted to 'reliability' and 'security of supply' rather than a dated discussion about 'subsidised renewables'.

I have watched the subsidy debate mature over the past 20 years. When fundraising in 2010 for one of the first solar funds in the US market tailored for institutional investors, more than 85 percent of investors came from outside the US. The primary concern of US pension funds that didn't participate at the time was the subsidised nature of renewables and their concern that it was an unsustainable business model. That thesis has been turned on its head and is now applied to coal, the owner/operators of which are wanting subsidies to help them compete with renewables.

We seem to have come full circle in a very short time. Nevertheless, renewables and lower-carbon power technology must address the reliability risks posed by their intermittency. This, more than President Trump, is the true speed bump the industry faces. Batteries have recently emerged as the likely saviour. If true, we will all look back at President Trump's policies in time and remember them as simply representing the death throes of a terminally threatened industry that became outdated.

We can already see that possibility based on cost issues alone, irrespective of the climate pros and cons. These types of fundamental economic transitions can be brutal, both financially for incumbent businesses and also, at a very human level, for the workers they employ. Therefore, Trump's ideological resistance and policy direction may not be that surprising.

SPOILING THE PARTY

But what can President Trump really do to ruin the renewables party? Renewables are largely regulated at the state level, which is important, as we have seen. Practically speaking, there are two key areas that investors are keenly observing and will remain vigilant about for the rest of Trump's term in office.

The first is federal tax policy, which can impact renewable investment directly by changing the relative value a renewables project can enjoy through the monetisation of tax credits and the current accelerated depreciation benefits. In short, a change in the corporate income tax rate can impact the cost of capital for equity invested in new renewables projects.

That may result in the need for pricing increases to drive the same rate of return, which, in turn, may slightly impair the cost competitiveness of renewables over the short term. In practice, however, most US renewables projects approaching construction today are already factoring tax reform into their investment evaluation, such that the pricing impacts won't be that material.

Secondly, a more serious but also short-term threat, is the outcome of the much publicised Suniva trade case, which should be known around the time this article is published. Should the decision favour the applicants, then all eyes will be on President Trump and what he elects to do. Will he impose punitive tariffs on imported solar modules to the US and crimp one of the greatest new job creators in the country?

The president can, should he wish, put some 'lead in the saddle bags' of US solar projects by increasing the cost of key equipment. While limited to solar, this is the highest growth sector of US renewables investment and so this is a big deal.

This will be a true test of ideology and politics over imperatives for ongoing economic growth and job stimulus and a real test of the president's energy policy conviction.

The outlook for US renewables infrastructure investment is positive despite the election of President Trump and investment flows are reflecting that. While the risk/return proposition in renewables is changing as the power industry evolves to accommodate new technology such as batteries, demand response, customer aggregation, electric vehicles etc., the opportunity set can offer some attractive strategies for institutional investors.

But, like any asset class, you need to be differentiated and ahead of the curve in order to prosper long term. There is no doubt, however, that investors making allocations to real assets and infrastructure strategies will continue to see renewable energy infrastructure front and centre in the alternatives presented to them by the growing cabal of GPs now becoming 'clean energy experts'.

Whether President Trump maintains his current policy position will, at the end of the day, have little impact on US renewables growth. ■