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PERSPECTIVE RENEWABLE ENERGIES



THE ENERGY TRANSITION STARTS IN OUR HEADS





MICHAEL EBNER
MANAGING DIRECTOR FOR INFRASTRUCTURE
KGAL INVESTMENT MANAGEMENT

Greta Thunberg, #FridaysForFuture and climate protection currently receive much attention. Greta is cheered on, we point an accusing finger at others, and yet people still buy strawberries in winter. In the current debate on climate protection, two different yardsticks are used. We criticise other people's behaviour, but have a blinkered view of our own behaviour, seeing only what we want to see.

I see three reasons for this: the complex nature of the topic, modern means of communication and our own complacency. As climate protection is a global issue, the debate soon becomes a fundamental one. But because the arguments are so convoluted, discussion is difficult and largely unsatisfactory for all involved. What is more, social media make it possible to engage in a simple, quick and protected way. It's all so easy: a post showing solidarity with a cause is written from the comfort of the sofa, an online petition shared at the click of a button. 280 characters are sufficient to air one's views, but are too few to analyse complex interrelationships. And because it is so hard to shake habits, we are ultimately prevented from acting in a sustainable way.

This gives rise to a conflict of interests, which is neither perceived nor contested. People are happy enough to enjoy the benefits of climate protection policy, but at the same time won't accept any restrictions to their life style. But that just isn't going to work. If we really want to protect the climate, we must change our behaviour and leave our comfort zone. It will not be enough to compensate one's own carbon footprint with a modernday "sale of indulgences". Those who purportedly want to

increase the share of renewable energies must accept the presence of wind turbines in their immediate surroundings. Every one of us must make a sacrifice in one way or other. The sheer enthusiasm expressed by millions of people towards initiatives such as #FridaysForFuture is amazing as it shows just how interested and concerned people are. A true movement can now be seen: indeed, supporters of #FridaysForFuture are taking to the streets and are willing to accept restrictions to their lifestyle. A change to people's mindset and behaviour must now come about. Politicians must think ahead, take the initiative and back this change in people's thinking by passing the relevant laws. They cannot continue to be all things to all people if the energy transition is to succeed.



» IF WE WANT TO PROTECT THE CLIMATE, WE MUST CHANGE OUR BEHAVIOUR.

» FOR THE ENERGY TRANSITION TO SUCCEED, POLITICIANS CANNOT CONTINUE TO BE ALL THINGS TO ALL PEOPLE.

A photograph of several offshore wind turbines in the ocean under a bright sky with scattered clouds. The sun is low on the horizon, creating a shimmering reflection on the water's surface. The turbines are silhouetted against the light sky.

ALEXANDER RIETZ
PORTFOLIO MANAGER
KGAL INVESTMENT MANAGEMENT

GO AGAINST THE FLOW TO GET AHEAD OF THE MARKET

The KGAL ESPF 4 renewable energies fund totals €750 million. With 32 institutional investors from 13 countries, it reflects the internationalisation of KGAL. Portfolio Manager Alexander Rietz is responsible for the investment strategy and its implementation; he knows the sector inside out.



Mr Rietz, you studied economics with a focus on finance. Where did your interest in renewable energies come from?

My first job after university was in Siemens' venture capital unit. I analysed the energy and environmental technology sector and invested in technology start-ups, which in the early 2000s were mostly companies that were conducting R&D in renewable energies. That primarily meant innovative module technologies for photovoltaics, control software, and new approaches to wind turbine design. I developed a keen interest in it, and that has remained with me ever since.

KGAL ESPF 4 closed at the end of September 2019. Did you celebrate with your colleagues?

We did celebrate the first and the second closing. Those were the big, important milestones that represented the validation of our strategy and the internationalisation of the fund – as well as of KGAL. Now we are immediately moving forward with the allocation of the capital raised.

And what does that mean?

It means being really close to the assets. We have concluded the first transactions and are keeping a close eye on their performance, while at the same time we're also continuously improving investor reporting. Moreover, two of the projects we acquired are in the construction phase, which is significantly more time-consuming than overseeing a project that is already in operation. These issues were ranked as a lower priority for me during placement of the fund.

Keyword: marketing. Financial investment in renewable energies is less familiar to investors than the stock markets. What was the question you heard most often?

That would be the question about our fund strategy – and we noticed that our explanation was well received. Right afterwards came the question of risk mitigation: how we manage risks, and what know-how we deploy. KGAL has built up its expertise over many years and we needed to communicate that properly.

The renewable energy market in Europe is quite diverse. Where is it stagnating, and where is it growing?

The market is very dynamic, so I can only give you a snapshot. There is currently plenty of activity in southern European countries where there is a lot of sunlight, and in Scandinavia where the wind resources are very good. We're closer to the market prices in those places, and not dependent on government subsidies. That could mean that these markets become more regulated over time, due to more capacity expansions – in which case the focus would shift to the next country.

Which is?

We are observing that countries such as Poland, Hungary and Ireland support regulation in order to increase the competitiveness of renewable energies in their regions. That's how things look today, but tomorrow it could all be a completely different story.

How do you deal with that?

In a dynamic market, the challenge is to have an organisation that is able to react fast. Metaphorically speaking, we're standing right outside the door so we can walk through the moment it opens.



» IN THE MEANTIME, RENEWABLE ENERGIES ARE PROFITING FROM SIGNIFICANT SCALE EFFECTS.



» **REGULATION IS IMPORTANT TO LONG-TERM PLANNING.**

» **I HAVE TO BE OUT IN THE MARKET AND TALKING TO PEOPLE TO KNOW WHICH WAY IT'S GOING.**

What role does regulation play? It's not unheard-of for laws to be changed retroactively.

Investors value long-term secure feed-in tariffs, but at the same time want to avoid high regulatory risks. However, fewer and fewer countries in Europe are offering government-imposed feed-in tariffs, with the effect that feed-in compensation falls significantly, or may even be awarded by means of competitive auctions.

What do you think of this development?

I think it's positive. As a Portfolio Manager, I can look at it pragmatically, and from the investor's perspective. We've moved away from a subsidised market and are operating in a more competitive way, right up to selling electricity via the spot market. We're trying to find a middle course.

By...

...structuring long-term power purchase agreements, but also trying to profit from the upside potential of the market. It's about not putting all your eggs in one basket, which means combining various purchasing mechanisms into a single portfolio to achieve an appropriate yield/risk profile.



» **GREENFIELD INVESTMENTS ARE INVESTMENTS IN THE PLANNING OR CONSTRUCTION PHASE.**

» **BROWNFIELD INVESTMENTS ARE EXISTING PROJECTS THAT ARE ALREADY IN OPERATION.**

You've just described diversification again. Does that also explain why the KGAL ESPF 4 investments are so internationally distributed?

That is an approach that we take to achieve stable cash flow, and it's one of our core messages when talking to investors. We've learned some lessons from the past: with a broad, internationally diversified portfolio, we can better absorb the impact of regulatory changes or performance fluctuations.

The sector has evolved – has this also had an influence on investor appetite?

As trailblazers, we've enjoyed a good vantage point on this, and can say that attitudes to renewable energies have changed radically. It used to be that we mainly dealt with German clients, but now three-quarters of KGAL ESPF 4 investors are from outside Germany. They realise that they can achieve stable, attractive profits and simultaneously address the sustainability issue. That's really noticeable.

How does the strategy pursued by KGAL ESPF 4 facilitate a stable yield?

By bringing two different worlds together. We are structuring the KGAL ESPF 4 portfolio in such a way that a basic yield is provided via brownfield investments – in other words projects that are already in operation. At the same time, we are acquiring investments that are still in the project development or construction phase: "greenfield" investments. Those investments enter the yield phase later, but offer higher return potential.



How do you make attractive brownfield investments in the current market environment?

As an example, we invested in an offshore wind farm in Germany. This technology is well-established, but harder to manage than photovoltaics or onshore wind. That is usually accounted for by an increase in yield.

How do things look abroad?

The fund acquired a photovoltaics portfolio in Bulgaria. Everyone is very familiar with photovoltaics, but not with Bulgaria – so a yield premium is anticipated here as well. We were also able to structure new debt financing at considerably better conditions.

You refer to the combination of greenfield and brownfield investments and define it as the intersection of the market and the customer's requirements. That makes it sound easy!

Sure, but it requires a lot of experience. You really have to read the market, draw the right conclusions, and specifically seek out differentiation. You have to go against the flow to get ahead of the market.

In fact, a three-dimensional matrix incorporating technologies, regions, and investment phases is also applied at the intersection point...

...along with additional conditions such as the proportion of foreign currency or financial leverage, which are negotiated individually. In reality, there are even more dimensions.

Do experience and networking also play a role here?

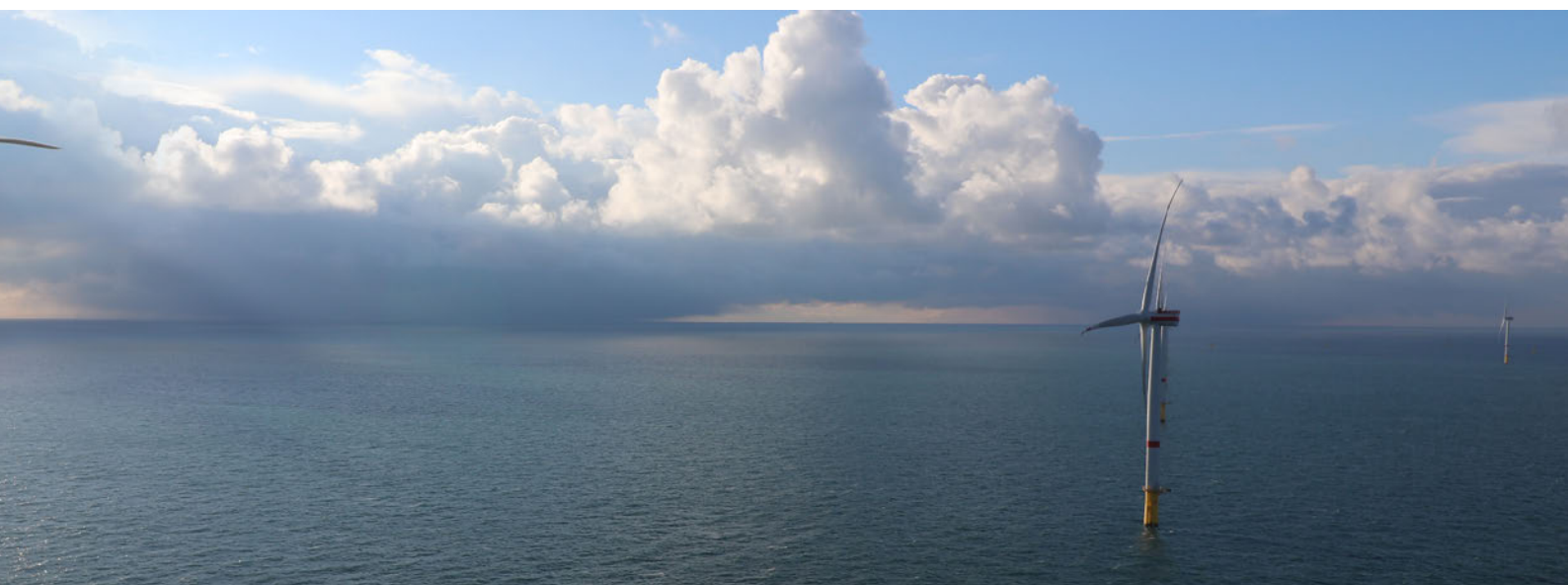
Yes, though that is sometimes hard to put across. When investors ask what makes us stand out, we say: "We've been on the market a long time and have better access to transactions". That can't really be quantified, but investments in renewable energies are far more than just a financial model.

There is even a social component, because you're generating environmentally friendly energy. Do you want to change the world?

It's important to me to enjoy my work. Looking back over the years I can see that it's possible to make a change, and of course it feels good to generate benefits for society. A lot of my friends think what I do is great.

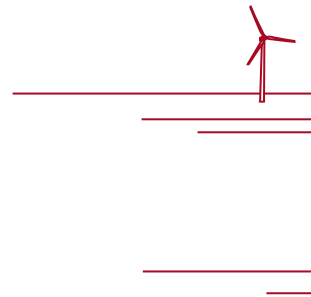


» **PERSONAL APPRAISAL IS IMPORTANT BECAUSE IT'S BASED ON KNOWLEDGE AND EXPERIENCE.**



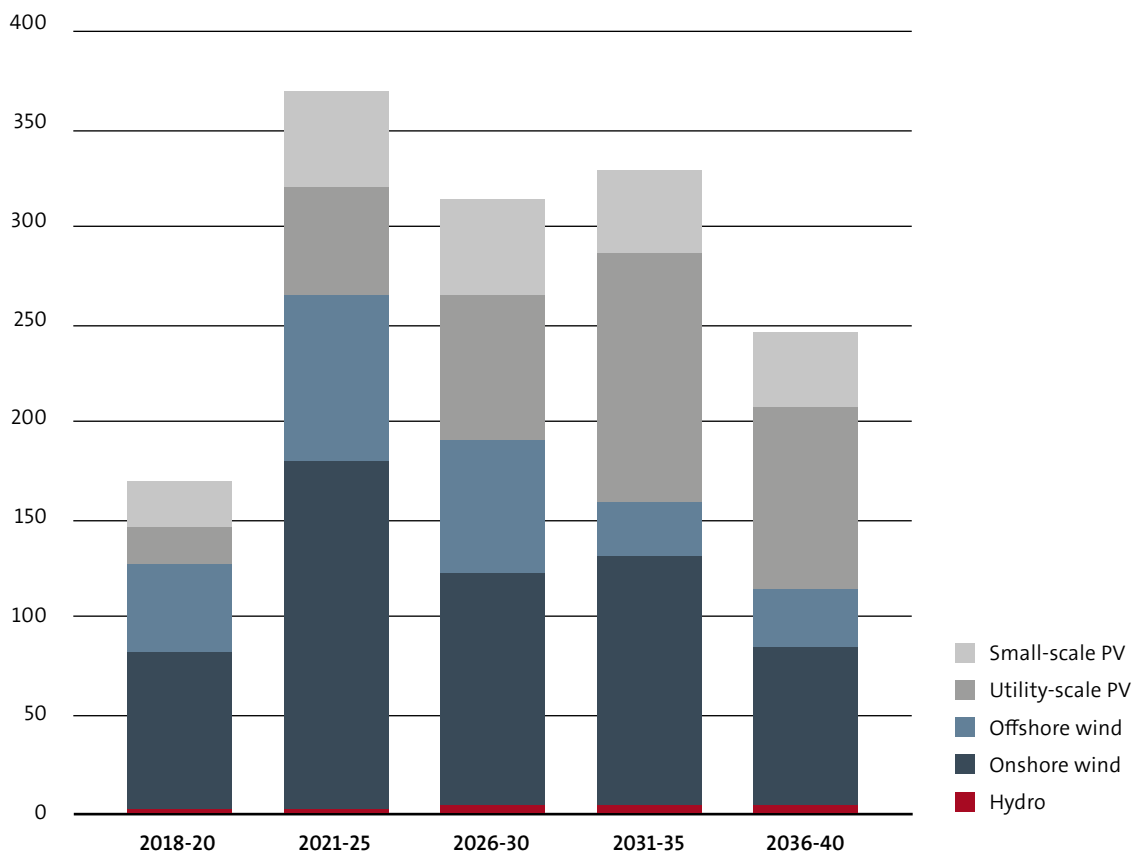
“IF SOMEONE WALKS IN WITH A SOLAR PROJECT TOMORROW AND IT TAKES A BILLION DOLLARS OR THREE BILLION DOLLARS, WE’RE READY TO DO IT, THE MORE THERE IS THE BETTER.”

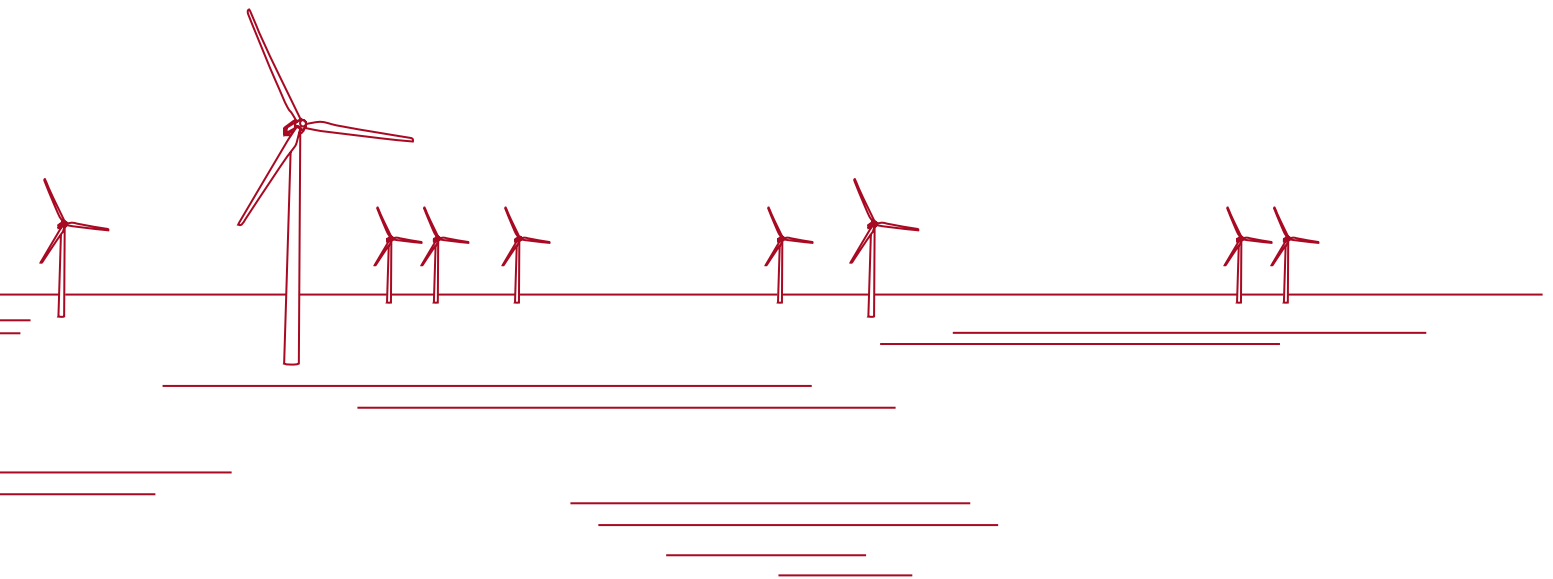
WARREN BUFFETT¹



AT A HIGH LEVEL: INVESTMENTS IN RENEWABLE ENERGIES

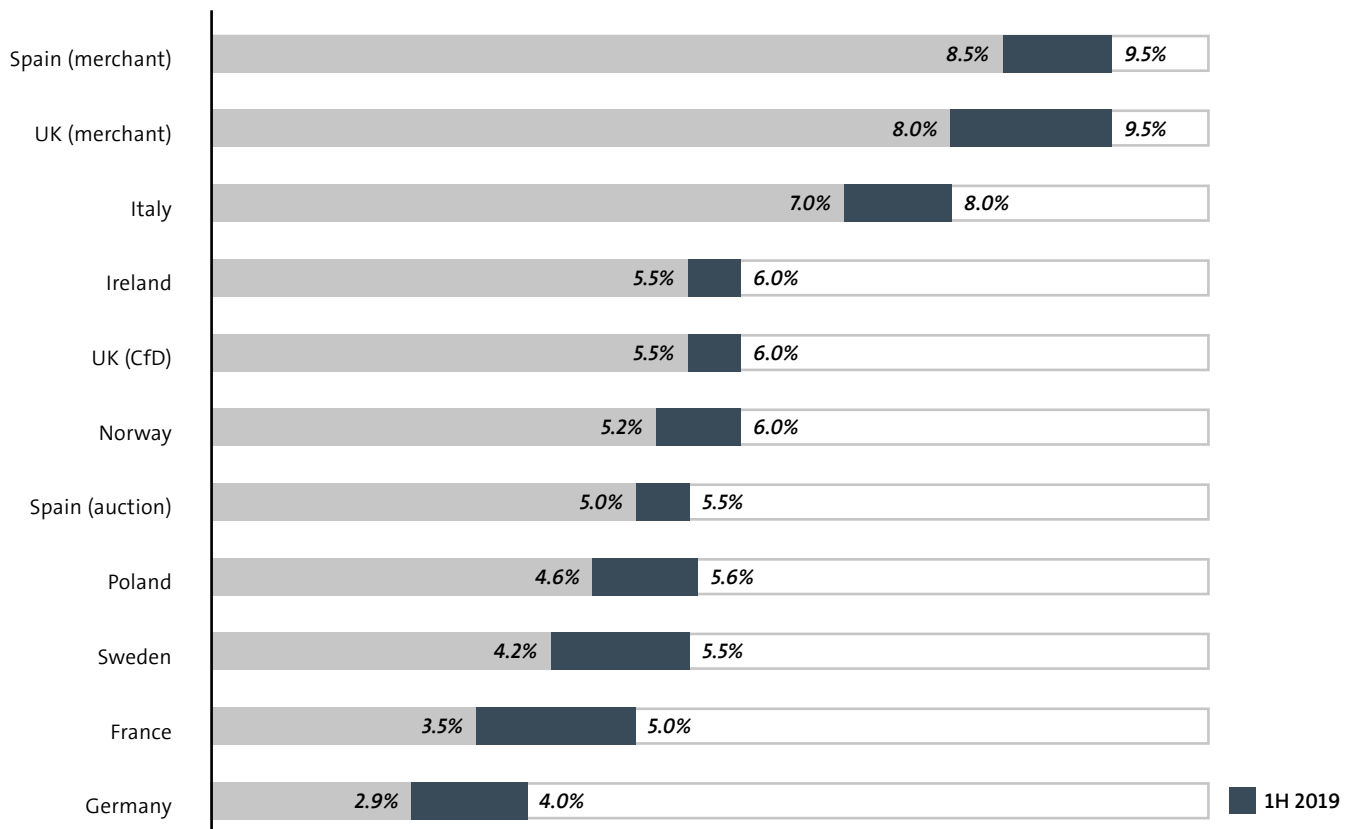
Annual investment by technology in billions of dollars²





THE EXPECTED RETURN REFLECTS THE HETEROGENEITY OF THE MARKET FOR RENEWABLE ENERGIES

Institutional investors' unlevered equity return expectations for commissioned assets (%)²



SAVOIR - VIVRE RESPONSIBILITY SOPHISTICATION & ENJOYMENT



Faire ou ne pas faire – what do you need to know about living and working in France? Our Asset Managers in the KGAL Investment Management France team – two French, two German, and one Catalan – look after 25 investments, and are very well acquainted with the country. These are their observations for doing business and for fans of the French way of life.



Oliver Stapelfeldt – Asset Manager

AN ELEGANT CONCLUSION

I like that the French combine work and pleasure. Meetings are often rounded off over a delicacy such as a macaron.



Sylvain Cotta – Asset Manager

APÉRITIF DÎNATOIRE – TO NURTURE AND MAINTAIN YOUR FRIENDSHIPS

If a group of six or eight people meet for an apéritif dînatoire (drinks and nibbles), you can expect plenty of chat and discussion – even about politics. It's par for the course that sometimes voices are raised a little, but it's soon all forgotten again.



Daniel Meyer – Asset Management Team Leader

HONOUR YOUR CLOSEST TIES

Eating together is important, mainly as an opportunity to meet up with family, relatives and friends. Major celebrations start with an aperitif at lunchtime and the rest of the day is spent together.



- ◇ Fools rush in. Whereas Germans get straight to the point, the French value a more subtle preamble.
- ◇ Pay respect to French culture. The French are proud of their country.
- ◇ Be tolerant. There is a real awareness of responsibilities, even if people are not perfectly punctual.
- ◇ Be accommodating. Take a relaxed and friendly approach to scheduling meetings.
- ◇ Opt for a modest appearance. Status symbols are of less importance.



Antoni Güerre – Asset Manager

A MACARON IS A HIGH-TECH PRODUCT.

A macaron is not easy to make – it is a sophisticated treat. It is intertwined with French culture, with a focus on enjoying life.



Heiko Bucke – Asset Manager

THE LOVE OF LANGUAGE

French contracts, small talk in French, and French radio in hotels: the French love their language and cherish it perhaps more than any other nation. It's quite evident everywhere.

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KGAL Group

KGAL's investments in renewable energies focus on a diverse portfolio in the wind power, photovoltaics and hydropower sectors. Since the turn of the millennium, the company has invested in more than 130 assets across Europe with a total volume of approximately €2.8 billion. KGAL Group is a leading, independent investment and asset manager with an investment volume of around €20.5 billion. The investments focus on long-term capital investments for institutional and retail investors in the real estate, infrastructure and aviation asset classes.

Sources:

Images: *Veja Mate Offshore Project GmbH*

Cover image: *Offshore wind farm Veja Mate*

Warren Buffet Quote: ¹ <https://cnb.cx/2zPStvL>

Charts: ² *Bloomberg NEF New Energy Outlook 2018*

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