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Despite Energy Turmoil, Renewables Are Gaining Traction

Analysts increasingly see wind and solar as part of a mainstream investment mix. Nuclear, while carbon-free, remains problematic.

By Laurie Wiegler February 25, 2016

Despite Energy Turmoil, Renewables Are Gaining Traction

Whether investors know the details of the landmark carbon emissions-capping accord signed by 195 countries in Paris in December or not, it's probably clear that the investment climate for clean, renewable energy has shifted.

Wall Street analysts increasingly agree that putting renewables like solar and wind into the investment mix makes business sense, though near-term expectations should be restrained. Oil has recently slipped below $30 a barrel, whereas solar and wind are just becoming more profitable, albeit with unpredictable returns. A third noncarbon sector, nuclear, however, presents a more complex commercial picture, particularly after the March 2011 Fukushima Daiichi meltdown, when countries that had once embraced the technology, such as Japan and Germany, turned to solar instead.

Solar has been ascending despite choppy markets. Elon Musk, founder of Palo Alto, California–based carmaker Tesla Motors and private rocket maker SpaceX, in Hawthorne, California, is also chairman of San Mateo, California–based SolarCity Corp. Musk's solar start-up, which went public in December 2012, offers the long-term potential of marrying solar and wind-generated power with advanced storage capacity — batteries — that he pioneered at Tesla. SolarCity, which is losing money, is too risky a bet for many analysts, though they find the technology intriguing. "There's a drive to try to mix renewable resources with storage, which means battery technology from companies like Tesla, which would make solar and wind a more valuable resource; [the battery] can produce at night even if a cloud comes overhead," says Patrick Jobin, a Credit Suisse equity analyst in New York.

Krish Sankar, an analyst with Bank of America Merrill Lynch in San Francisco, says solar-distributed generation, which is decentralized power connected by microgrids, is "very strong" in the U.S. SolarCity has been installing solar panels not just in homes but also in retail locations and schools; the company, for instance, has a project putting solar into Walmart locations.

And SolarCity has attracted considerable investment support. “Institutional ownership has broadened quite a bit over the past year, and active institutional ownership (excluding index funds and broker-dealers) rose from approximately 35 percent to 40 percent of shares outstanding from 2014YE to 2015YE,” SolarCity spokesman Jonathan Bass wrote in an e-mail. “Large institutions have also invested in our asset-backed securitizations.”

Still, SolarCity’s stock, like most energy plays, has been pummeled in recent weeks, driven in part by falling energy prices. On February 22 SolarCity closed at $19.08, down 68 percent since mid-December.

Analysts argue that renewables shouldn’t be damaged by dramatically falling oil and gas prices. “Many investors tend to correlate oil and solar, but [oil] doesn’t have an impact [on solar],” Sankar says, even though he adds that lower natural-gas prices do affect utility-scale solar projects. “Margins have come down as natural-gas pricing has come down.” Some investors, he adds, “want to rotate out of growth stocks and into cyclicals. And solar is largely viewed as a growth sector.”

Credit Suisse’s Jobin agrees that there is “no correlation of equities” and adds that “it hurts sentiment, however, under the somewhat naive assumption that low oil prices mean solar is all of a sudden not an economic buttress.”

Jobin says the renewables sector, particularly wind and solar, is very “capital intensive — and requires significant capital raising,” whether from private and public equity, corporate debt, securitizations or project finance. “What that means,” he says, “is there’s a relationship between cost competitiveness and the interest rate environment, and whether capital markets are open for capital-raising in segments renewable developers use.” Recent market volatility and the possibility that the Federal Reserve will continue to hike interest rates have significantly reduced corporate debt issuance.

Sankar says investors have been very cautious about solar. “In Japan,” he says, “there was a pickup [of solar power] after the nuclear disaster, and in the U.S. you see a favorable policy environment."

Investors also show some trepidation investing in wind, despite the fact that more advanced turbines have been developed and installed worldwide. Jeff Roberts, a senior scientist and deputy program director of energy at Lawrence Livermore Laboratory, points out that 100-kilowatt wind turbines in outlying areas of the lab's San Francisco suburb — once a common sight on the parched brown hills off Interstate 580 — are old news. New, masted turbines, which tower 70 feet above the ground, operate at 2.3 megawatts. "One new turbine could replace 23 of the old turbines," he says.

Roberts notes that in some areas of the U.S., wind energy represents as much as 16 percent of overall energy consumption. According to figures from Lawrence Livermore, at the end of 2014 wind use in the U.S. was just 1.73 of 98.3 total energy sector quads (each quad equals 10 BTUs), above that of solar, at 0.427 quads, but still dwarfed by nuclear at 8.33 quads.

Nuclear remains a clean (at least in terms of carbon production), if controversial, technology. Bruce Kahn, an analyst with New York–based institutional money management firm Sustainable Insight Capital Management, says, "Uranium prices are really low, but no new plants are getting built in the U.S., and there is a tremendous amount of fear about them. It's not something that is very attractive in any asset class if you are comparing [nuclear energy] to solar and wind."

But whereas the reactor boom has slowed, it's not over. A spokesperson with the Nuclear Regulatory Commission says there are a number of U.S. reactor projects under way. One, in Tennessee, has been licensed to operate; four are under construction (two in Georgia, two in South Carolina); and one has been licensed for construction and operation in Michigan.

Meanwhile, DTE Energy (formerly Detroit Edison) has yet to decide on starting construction, two reactors in Texas are awaiting a final NRC licensing decision, and seven more are "at earlier points in the NRC's review process," says the spokesperson.

At the same time, some reactors are being shuttered. Vermont Yankee shut down permanently at the end of 2014, while Pilgrim in Massachusetts, FitzPatrick in upstate New York and Oyster Creek in New Jersey have announced plans to close in the next few years.

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What does this mean for investors? They must choose between noncontroversial solar or wind, which often suffers from the not-in-my-backyard syndrome. Sustainable Insight's Kahn says returns can vary, depending on whether the company is a private equity investment or publicly traded. Rates of return also vary "by virtue of your expectations, the risk you are taking and length of time you have to put the money to work," he says. "Nuclear energy is a whole different ZIP code," he adds, and investors have to be mindful of the "regulatory environments" that accompany massive projects.

Public companies have been what Kahn calls a minefield, but the returns can be quite good. Another analyst says one downside of private markets is that they're less liquid. Limited partners invest through a sponsor, and the asset can be tougher to sell than if it were a publicly traded company. It helps to have better knowledge of the technology, be it nuclear, solar or wind, because you'll likely be holding it longer.

Still, Jobin says, investing in renewables remains strong. "If you look at the solar space overall for 2016, we estimate there will be about $90 billion worth of investments made in solar globally. Only a small portion will come from public markets," he says. "The lion's share of investments is still on the private equity side."

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