KEYNOTE INTERVIEW

A new paradigm

Energy transition is now a cross-sector investment theme rather than a siloed asset class, says Saket Trivedi, partner at Cube Infrastructure Managers

Q How is the energy crisis impacting the energy transition sector in Europe?

The energy crisis has revealed just how reliant we are in Europe on imported fossil fuels, which has resulted in the cost of living crisis that we are currently experiencing. These energy security concerns are creating renewed impetus around the energy transition sector and the need to ensure self-sufficiency when it comes to energy supply and distribution. Creating long-term sustainable infrastructure that can fulfil the dual objectives of reducing greenhouse gas emissions and achieving energy independence has therefore become critical.

Q What role does energy efficiency have to play in energy transition and how is this being highlighted by the ongoing crisis?

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Energy affordability is an important issue in today's world. Many of the companies we invest in have the ability to pass on fuel costs to end customers. District heating assets are a good example. However, while the cost of natural gas has averaged around €30/MWh over the past 10 years, in August and September of 2022, that figure reached €300/MWh.

There is a lot of literature explaining why that happened; pipelines were shut down, the market overreacted. What matters is that although we contractually have the right to pass on that 10-fold increase, that would be counterproductive if the end customer was not able or willing to pay. One of the most effective ways to tackle these challenges is through the implementation of energy efficiency initiatives that drive a sustainable reduction in the need for energy and, therefore, in customers' bills.

Q What impact is the current crisis having on LNG?

LNG has a very important role to play, at least in the short-term. When gas prices began to soar in Europe, it suddenly became economical to import vast amounts of liquid gas from North America and the Middle East. In fact, at one point, there was so much LNG coming to European shores that the price of gas became negative for a short while.

LNG has been extremely useful in restoring supplies lost from Russia and has helped gas prices come down. From €300/MWh in September last year, prices now stand at around €60/MWh today. That is still double the historical average, but it is a great deal lower comparatively. However, shipping vast amounts of gas across the globe is clearly not a sustainable option, and so we see LNG playing more of a temporary role.

Q What other solutions do you expect to take over from LNG in the longer term?

While LNG has been a great short to medium-term fix, preventing customers from facing excessively high prices, in the long term it isn't the answer. Ultimately, we expect to see a significant substitution of gas, in general, by electrification, renewables, biomethane and eventually hydrogen.

The electrification trend is already well underway. Electric vehicles are proliferating and Cube, for example, has already invested in a number of EV charging companies. We are also investing heavily in the electrification of our bus assets.

Meanwhile, renewables will increasingly replace gas as a source of that electrification. Wind, solar and other renewable technologies have become increasingly affordable, meaning renewable generation is displacing old, combined cycle gas turbines at an increasingly fast rate.

Biogas, meanwhile, has been around for some time, but given the current energy security situation, governments across Europe require significant additional investment in this space. Biomethane is a form of biogas with the impurities removed, meaning it can then be injected into the gas grid. Finally, in the long-term, hydrogen is going to play an important role replacing natural gas. LNG is great as a stop gap, but these four trends are what will really make the difference.

Q Which areas within the energy transition market is Cube focusing on and why?

On the supply side, we continue to be active in traditional solar and wind assets. Having said that, we tend to focus more on platform opportunities, working with management teams to help us buy and grow rather than just acquiring single assets. We are also looking at the next generation of energy supply including battery storage, hydrogen and biofuels, although many of these technologies are still at an early stage.

We are looking at biomethane, which has received renewed impetus as a result of the energy crisis. We are currently looking to make an investment that will involve using not just organic waste, but other forms of waste – municipal solid waste for example – to produce natural gas that can be injected into the gas grid. We hope to complete this deal early this year.

On the demand side, meanwhile, we continue to be interested in district heating, particularly given that 80 percent of European household energy consumption involves heating. Reducing operating costs in the face of rising prices is therefore a top priority for local authorities.

However, while we were early movers in the space with a first investment back in 2010, the interest for these assets has significantly increased since then. In order to avoid that competition, we started looking at smaller assets, for example in Northern Italy, where we have made a series of acquisitions. We have combined those assets to create CogenInfra, a larger district heating business comprised of several networks across the region.

Another portfolio example is a district heating business we have recently acquired that supplies 15 municipalities across the Czech Republic, which is a market with a stable regulatory environment. We continue to look at opportunities in the energy efficiency space as we strive to reduce energy consumption for end customers.

Q How do you decide when it is the right time to invest in these newer technologies and use cases, particularly hydrogen?

Cube is first and foremost a brownfield infrastructure investor, so we are naturally constrained when it comes to investing in early-stage technologies. However, when it comes to timing, what matters is that we have strong conviction with regards to the predictability of future cashflows. That predictability can be achieved in many ways.

The most common way is via a long-term contract or offtake agreement. That gives us comfort, even if the technologies are less mature. In fact, predictability of cashflow has sometimes little to do with the relative maturity of the technology. There are well-documented examples of proven and mature technologies generating unpredictable cashflows. It is that predictability that defines when the right time to invest is.

Q What makes the energy transition market attractive for investors?

There are three main reasons why the energy transition market is attractive for investors. Firstly, there is significant amount of legacy infrastructure that needs replacement and upgrading. There are still 40GW of coal-fired power plants operational in Germany, for example. There is also a significant amount of nuclear assets that need to be shut down in some countries including Germany and the UK. The upgrading of that old infrastructure is not just being driven by economic activity, but also by environmental and social concerns. This creates investment opportunities and makes the market attractive for investors.

Secondly, there is significant political impetus behind energy transition. There was a point in time when we had green political parties and political parties that were more circumspect about the need to tackle climate change. Today, there is bipartisan support for energy transition in most countries across Europe and investment in this space is deemed essential.

"The energy transition today is an all-pervasive theme rather than a sector with strict boundaries"

Indeed, a significant amount of investment has already been made. More than €200 billion was invested in the energy transition in Europe in 2021 alone. The latest EU roadmap for achieving net zero by 2050 relies heavily on private sector investment to increase renewables capacity by 40 percent and continue evolving nascent sectors including battery storage and hydrogen. The political impetus also makes this an attractive market to invest in.

Finally, of course, what makes a market attractive is the potential returns. The energy transition is still able to deliver that financial performance, particularly if, like Cube, you are an early mover. We were early movers in the district heating market, for example, with strong exits including Idex. We were also an early mover in the waste-to-energy sector, with successful exits under our belt including CNIM Development. Meanwhile, our renewables investments have also served us well with exits including RPIPE, Fotosolarium and Boralex.

Q How does Cube's broader infrastructure experience support its approach to investing in energy transition?

Energy transition is becoming an asset class in itself. Just as you have real estate, hedge funds, private credit, private equity and infrastructure, you also have energy transition, which spans all of those industries. In our own portfolio, for example, energy transition overlaps with digital infrastructure and mobility. A recent example would be the electrification of buses in our public transportation business. We also see an overlap with assets such as our EV charging business Stations-e and digital network operator Heliot Europe. Energy transition today is an all-pervasive investment theme rather than a sector with strict boundaries. ■