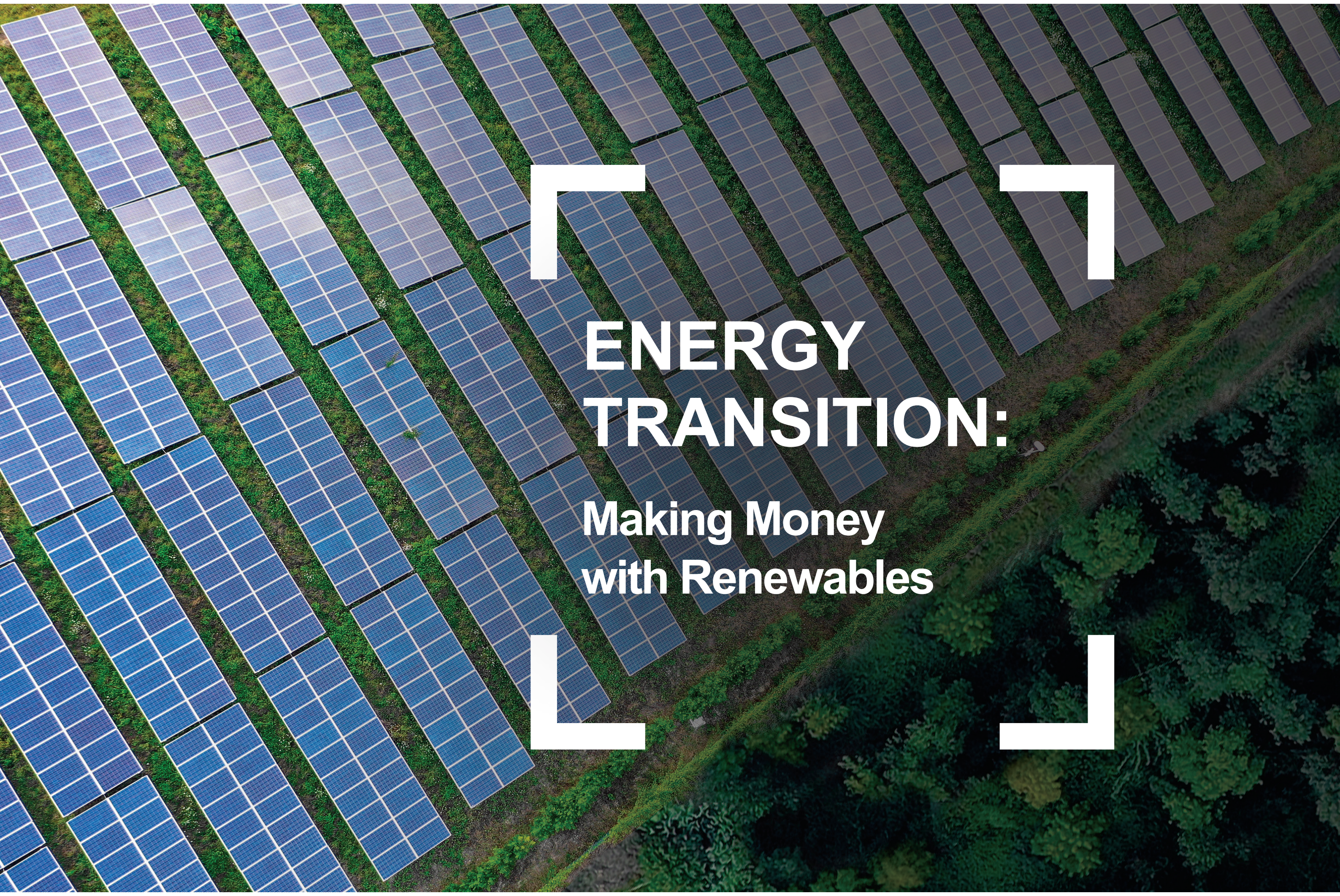
COMMENTARY



ENERGY TRANSITION:

Making Money with Renewables

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Marakon

Management Consulting at Charles River Associates

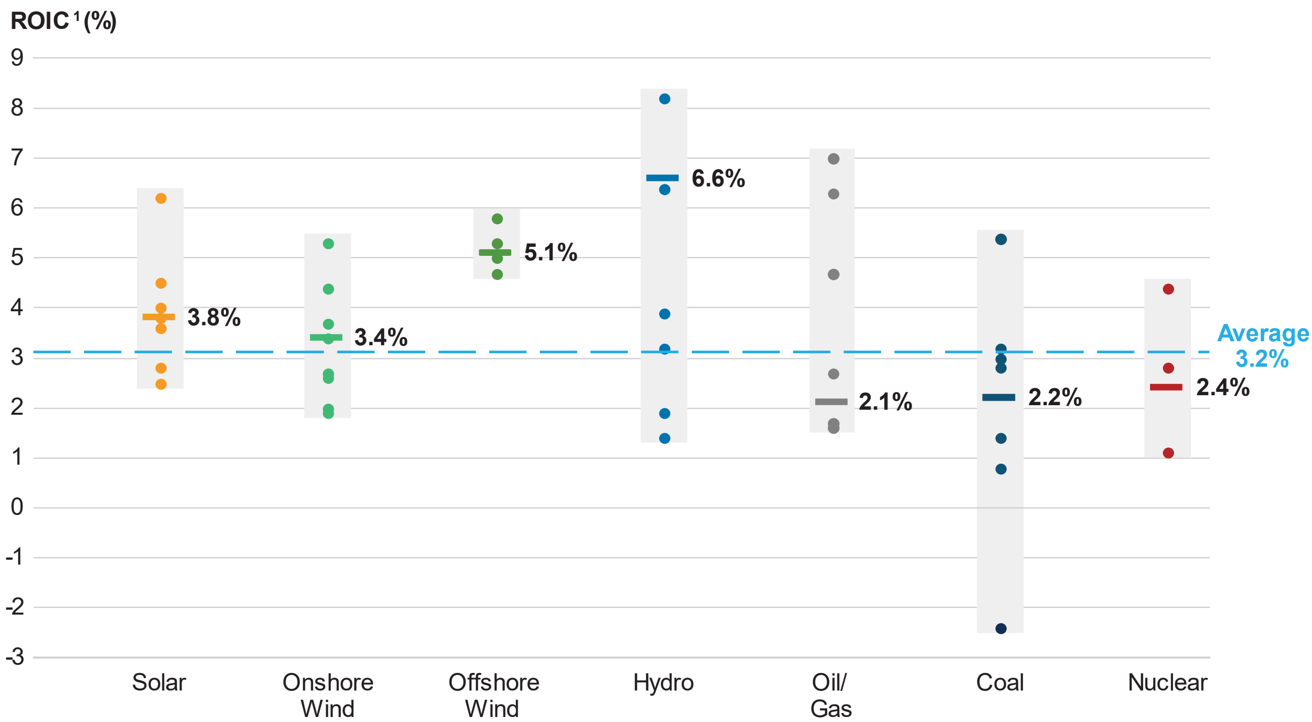
As the world transitions to renewable sources of energy, we see substantial growth for some power sources and decline for others. This places pressure on players invested in traditional power sources to change and provides opportunities for new entrants and expansion plays. Recent evidence suggests that money can be made in renewables – but not by everyone. Financial success will require selecting the correct mode of entry and building a focused strategy to create competitive advantage in the market.

Money is being made in renewables, but not by everyone

In the last four years, renewable sources of power (including hydro) have offered better returns than other power sources (Exhibit 1). Reflecting on the strategic choices individual players have made, there is significant variation around the mean for each power category.

In solar and onshore wind, the biggest producers have lower returns, partially compensated by a lower cost of capital. Meanwhile, offshore wind is a smaller playing field where those who overcome the entry barriers realise higher returns on average.

Exhibit 1: Average returns of public utilities globally by primary source of energy



[1]Weighted average of 2017–2020 returns of 44 pure players and reported business segments globally, assuming tax rate of 37.5%
Sources: IEA, Cap IQ, Company websites

Key: ● Companies considered
▬ Average for the energy source

Organic entry is feasible, but good returns are not guaranteed

The growing renewables market provides space for new entrants. However, extending or building competitive advantage and creating value is hard. Successful new entrants will need to leverage at least one of the following drivers of excess returns.

- **Local context and access:** Leverage deep knowledge of local operating environments and existing relationships.
- **Operational capability and synergy:** Achieve efficiency in operations based on existing technology, engineering and co-located operations.
- **Financing:** Use a strong balance sheet and diversification benefits to invest at a lower cost of capital.
- **Timing:** Enter when a new technology is maturing, and scale plays become feasible with ample headroom for growth.

Inorganic entry is an option, but the path to value creation isn't obvious

Acquisition as a route to enter the renewables market may lower some of the risk an entrant faces, but without clarity around the value-add to the target, value creation will remain elusive. Apart from lower cost of financing and potential true synergies with existing operations, it may be worth considering other avenues to increase the odds of value creation:

- **String of pearls:** Build a strategy for a targeted sequence of deals that complement the existing business rather than acquiring a single, large-scale player.
- **Basket of bets:** Take stakes across multiple power generation sources and geographies to minimise idiosyncratic risk.
- **Coalition play:** Partner with technology and infrastructure companies to widen the aperture on investment options and potentially access underperforming, and likely undervalued, targets.
- **Early project entry:** Leverage superior risk management or tolerance to lower premiums by buying an asset earlier in the development process.

Winning in renewables takes a deliberate strategy that builds on company assets and capabilities and extends current sources of competitive advantage into the market.

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About Marakon

Marakon is a strategy and organisational advisory firm with the experience and track record of helping CEOs and their leadership teams deliver sustainable, profitable growth. We get hired when our client's ambitions are high, the path to get there is not clear (or taking too long) and lasting capabilities are as important as immediate impact.

We help clients achieve their ambitions for sustainable, profitable growth through:

- Stronger strategies and advantaged execution based on:
  - A better understanding of what drives client economics and value
  - Insight into changing industry dynamics and the context in which clients need to succeed
- A stronger management framework to generate better ideas and link decisions and actions to value
- A stronger organisation with a more focused top management agenda and well-aligned resources
- A more confident and effective leadership team that's focused, decisive and strategic

We have a joint team delivery approach where client ownership and engagement is paramount. Partners are highly engaged in the work product and supported by strong analytical and industry relevant capability. We work as advisers and catalysts in close, trust-based relationships with top management teams.