Yieldcos: going, going, gone?

Rene Lavanchy

18/10/2017

On 16 October, Brookfield Asset Management subsidiaries closed on the long-awaited deal to up their parent company's stake in the developed market-focused yieldco Terraform Power to 51% and take over sponsorship of the company from bankrupt SunEdison.

If Brookfield is successful, and market rumours are confirmed, the asset manager looks set to pull off a trio of yieldco acquisitions this year. Brookfield has already agreed to acquire 100% of emerging market-oriented Terraform Global, and that deal is scheduled to close in the fourth quarter of this year. Meanwhile, Brookfield has also been linked with the outright acquisition of Atlantica Yield, the formerly Abengoa-sponsored yieldco.

Moreover, two more yieldcos are currently up for sale: 8point3 Energy Partners, in which both major shareholders First Solar and SunPower are looking to divest, and NRG Yield, in which sponsor NRG Energy plans to sell between 50% and 100% of its 46.7% stake.

Survival of the fittest

However, there is no reason to assume that Brookfield would be a buyer for either yieldco. The asset manager has described the Terraform yieldcos as "distressed" assets in investor presentations, and has acquired Terraform Power at a discount of $1.17 to the trading price at the time of the deal being announced in March. Atlantica Yield is also constrained by the bankruptcy restructuring of its sponsor Abengoa, which hampers its ability to acquire projects.

8point3 on the other hand is continuing to acquire projects, albeit slowly, and spent $313 million on acquisitions in the first nine months of this year, compared to $124 million for the same period last year, according to its latest quarterly results. Most recently, in November 2016, it acquired a 34% stake in the Stateline solar project from sponsor First Solar. NRG Yield also benefits from a solvent sponsor, and Brookfield may, after swallowing two or three yieldcos, decide to pass on a fourth, especially as it is the biggest yieldco of all, with a market capitalisation of around $3.5 billion and over 6GW of generating assets.

Unfortunately for the yieldco model, such vehicles no longer look like attractive options for renewable energy developers to generate cash from their project portfolios. While 8point3 has acquired one project stake in the past 12 months, it has had to forgo the chance to acquire more. Earlier this year, First Solar agreed waivers with the yieldco over the Switch Station, Cuyama and California Flats solar projects, over which 8point3 had the right of first offer (ROFO). All three have now been sold – Switch Station to EDF, Cuyama to DE Shaw and California Flats to Capital Dynamics' Clean Energy Infrastructure fund.

Discussing the Switch Station divestment in a second-quarter earnings call, First Solar chief executive Mark Widmar reportedly said: "Following the receipt of a waiver under the ROFO agreement with 8point3 for interest in the Switch Station project, we were able to leverage the continued vigorous market demand for our high-quality systems projects and selling interest in Switch Station at a significantly higher valuation versus selling to 8point3".

Simply put, 8point3 was not able to make a competitive offer for the projects. Equity raises, the supposed backbone of yieldcos' acquisition strategy, have not been attractive. 8point3's stock price has been flat on average in the past year, defeating the hoped-for virtuous circle of rising stock prices allowing equity issuance to fuel further acquisitions, which would raise the price yet higher. No yieldco raised any public equity in the first quarter of 2017, unlike the first quarter of each year in their four-year lifespan, according to Bloomberg data. As a result, overall project acquisition activity has been subdued. Despite the size of its balance sheet, NRG Yield only closed one dropdown from its sponsor in the second quarter of 2017, a 25% stake in a wind portfolio for only $42 million. NRG Energy acquired a 1.5GW portfolio from SunEdison in 2016, but these have yet to be acquired by the yieldco.

"I think they've been in a holding pattern," one financial adviser comments. "I don't believe that the yieldcos have been especially active on the M&A front. They've been trying to clean up their capital structures. In the interim, you've seen a lot of institutional investors step up their M&A activity."

Funds pile in

Indeed, while yieldcos may have retreated from the stage, institutional investors have encroached. In February, Canadian pension fund manager Alberta Investment Management Corporation agreed to take a near-50% stake in sPower, one of the biggest privately held solar power developers in the US.

Allianz Global Investors, meanwhile, is increasing its deal-making capability in the US. In August, it hired Catherine Helleux from Societe Generale to work on renewable energy equity transactions. Later this year, chief investment officer for infrastructure equity Armin Sandhoevel will move to New York. "We are expanding our global infrastructure equity offering and bringing it to the US market," a spokeswoman said earlier this month, and renewable energy – mainly greenfield but also brownfield and re-powering deals – are a priority. Allianz is also planning to launch a renewables fund dedicated to the US this November.

With a lack of available capital and growing competition from the institutional market, it could be that yieldcos will themselves end up subsumed into portfolio companies of those investors. But not everyone is sure. "I wouldn't say it's definitively a failure of the structure... they could be back in the market in the near future, but they haven't been [active recently]," the financial adviser comments.