The seller's market

Secondary market | Following years of frantic consolidation, the UK's secondary solar market has begun to slow. Liam Stoker analyses what the future holds in store for the once-thriving market, and what's next for long-term asset holders

Credit: WeLink.

The 72MW Shotton Solar Park, pictured, is currently the UK's largest and was quickly snapped up by Foresight Solar

With more than 8GW of utility-scale solar having been built in the UK, it was only a matter of time until the secondary market took off.

What followed the country's hugely successful Renewables Obligation build-out period was akin to solar's own Black Friday. Investors, lured to the market with predictable and economically viable returns, rushed in with deep pockets and even deeper shopping trollies, flinging in asset after asset.

That spree created UK solar's own 'Big Four', namely Octopus Energy Investments, Foresight Group, NextEnergy Capital and Bluefield. Between them, they own more than one-third of the built utility-scale solar market in the UK, and that share is continuing to grow. Kareen Boutonnat, COO at prolific solar developer Lightsource BP, describes the market as being dominated by "a few very big players and a very long tail". *PV Tech Power* publisher Solar Media's in-house market research team puts the top 20 asset owners as holding in excess of 70% of the market, helped by readily available assets and willing money.

But after a strong few years of purchaser power, aided by a subsidy programme that unwittingly created a boom-and-bust model, the UK secondary market has undoubtedly swung in favour of the seller.

A seller's market

"It's a good market right now if you own an asset and you want to sell it," Ricardo Pineiro, partner at Foresight Group, one of the UK's largest holders of solar assets, concludes. Across various funds, Foresight Group has amassed a portfolio of operational solar farms with a capacity of almost 1GW, almost entirely purchased during a time when supply far outstripped demand. Foresight was joined by a handful of other listed funds and a few other investors as early adopters of UK solar.

As a result, prices were relatively stable and, as Pineiro says, comfortably within the parameters of what its listed fund was able to pay. But as the sector has consolidated and assets become less available, prices have trended upwards to such an extent that Foresight has found itself occasionally priced out.

"We have a very strict pricing methodology because our fund is listed. We noticed that for the wider tenders – the ones we knew were widely circulated in the market – we went from being selected for the second rounds and being a shortlisted bidder, to on some occasions being told our pricing was more than 10% off," he says.

Rather than just a fleeting occurrence, this would appear to be happening with increasing regularity, particularly on those portfolios shopped around the market.

Prime examples of this can be found in the sale of both the Terraform and Canadian Solar portfolios, which garnered considerable interest before being sold during auction processes to Vortex and Greencoat Capital respectively.

Other investors have bemoaned similar circumstances. Kevin Lyon, chairman at NextEnergy Solar Fund (NESF), another of the UK's top five solar investors, says that competition in the secondary solar market is now "substantial". While NESF is continuing to make investments in the secondary market, it's doing so amidst other interests too. And last year Bluefield Solar Income Fund said it was looking beyond the Renewables Obligation era to embark on an "asset management journey" to optimise the portfolio it has amassed.

"That's what we're seeing in the market at the moment. There is more pressure on returns if you're buying assets, and there's a more limited pool of assets as we've already seen a significant amount of consolidation," Pineiro adds.

Problem pricing

So what constitutes a fair price these days? It's difficult to say, with a range of moving factors contributing towards the going price for any asset on the market today, least of all the level of subsidy and build quality of the actual assets in question.

There has also been a considerable movement towards more institutional money flowing into renewables, which in itself has had an impact on asset prices. For some time the main investors in UK solar were listed funds and a handful of others, but there has since been a trend towards a new breed of investment, especially pensions funds. Cubico, the asset owner which purchased many of British Solar Renewables' assets, is backed by Ontario Teachers' Pension Plan, while more recently HSBC's UK Pension Scheme division handed Greencoat Capital some £250 million to invest in UK solar and wind farms. Lightsource has partnered with BlackRock, the world's largest asset manager, to invest £1 billion into UK solar.

The phenomenon of investors with a perceived lower cost of capital flooding the market has, according to Pineiro, "created a shift" in the market in terms of how much assets can change hands for.

Asset prices can also vary widely based on the debt structure used to acquire them, with the level of gearing – or indeed the use of an equity-based strategy to offset that altogether – affecting the level of returns, and therefore the price a potential buyer is willing to pay, achievable on any given portfolio.

As a result of all these moving cogs, it is again difficult to determine what constitutes a fair price and what's overpriced, but nevertheless there is almost certainly a trend upwards as the available pool of assets on the market has shrunk and appetite for infrastructure investments, solar and renewables in particular, has accelerated. Pineiro says that some assets that have exchanged hands recently are clearly outliers, remarking that even withstanding some uncertainty over their bid structure, it has been "difficult to understand" how particular prices have been reached.

This has led Foresight to pursue bilateral deals with vendors who want a quick, simple sale that doesn't drag out over the course of a six- to nine-month auction process. Such prolonged sales inherently involve more costs from an advisory perspective, with some vendors simply wanting a more streamlined, easy-to-navigate process.

But such sales are now harder to come by, and the market in itself is far more fragmented than it was before, when sizeable portfolios were sold in one transaction. Now, according to Pineiro, you'll be lucky to find a portfolio on the market that's 50 or 60MW in size, with NESF also bemoaning this fact. The likes of Foresight, NESF and Bluefield have all guided towards far slower growth in portfolio size in the future.

Boutonnat says that Lightsource BP is continuing to do due diligence on new deals, with the firm's chief executive Nick Boyle describing the process as more of a "drip" than a flood, despite retaining an interest in sizeable portfolios. "There will continue to be some sales in that market, but it's not a huge consolidation with big, big platforms selling," Boutonnat adds.

In the event of slow growth, high prices and a consolidated and richly competitive market, what is the future for built UK assets and indeed, potential new entrants?

The next steps

"There's a question mark over what's next," Pineiro says, indicating his belief that while the market will still retain a fair amount of liquidity and churn, appetite for renewables infrastructure is only growing within investor circles. In that respect, the boom and bust cycle that has often befallen many international solar markets – the UK included – has occurred at precisely the wrong time. "[It] always seems to be in the wrong cycle between investor demand and the availability of new assets," Pineiro says.

NextEnergy Solar Fund's most recent results disclosure, published in November 2018, revealed very much its direction of travel. Secondary market assets would remain of interest but on a smaller scale than before and further down the priority list. Instead, NESF's outlook guides towards increasing opportunities in bolstering the technical and operating performance of its existing assets, and optimising the revenues it derives from them.

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Asset holders are indeed becoming far more sophisticated with how the power they generate is sold, taking into account short- and mid-term power price curves to determine what the best course of action is. Recently, many investors have sought to arrange short-term power purchase agreements (PPAs) for a larger proportion of their asset base, hoping to achieve a more stable, non-ROC revenue stream given the relative volatility of the spot market.

Repowering, too, is on the cards. Pineiro says Foresight has examined the potential for repowering old(er) assets with new(er) panels to eke every last drop out of an asset's grid connection – an activity which the repeal of the European minimum import price (MIP) could render more financially viable – but this remains very much a watching brief. The UK government is also mindful of the repowering equation and this summer consulted on proposals to effectively cap an asset's subsidy-eligible capacity at that which was originally applied for.

Then there's the battery storage question, one which occurs on almost every investor's radar. Nearly all of the major investors in UK solar have either made their first forays into battery storage or insisted the technology remains under consideration but, as yet, barely any ROC-accredited sites have had storage retrofitted. This, Pineiro says, is due to complications with the overall operation of the site and how the grid connection is utilised, meaning that storage is "not a straight forward investment proposition".

But if the question is 'what to do when built assets are running dry?', the more established asset holders are increasingly landing on the same answer: just build some more.

Sans subsidy

The RO closed for good on 31 March 2017 and, since then, deployment of ground-mount, utility-scale solar farms has been all but stymied. Save for a few corporate PPA-backed projects and the first glimpses of subsidy-free developments, there's been little coming down the pipeline.

That all looks set to change in 2019, when the market looks set to burst back into life. *PV Tech Power* publisher Solar Media's in-house market research division is guiding for around 500MW of utility-scale to be deployed next year, triggered at least in part, ironically, by the funds who've made hay while the sun has shone in the secondary market.

NESF is to break ground on its first tranche of subsidy-free solar projects in the UK early next year and aims to deploy some 172MW. A host of other developers are busily getting their ducks in a row, bolstered by the MIP's repeal and mid- to long-term power price forecasts shooting skyward.

Pineiro insists the unsubsidised market in the UK remains "quite speculative" – "It will happen in the UK, but not quite yet," he says – but there are ample developers who do not share quite such a pessimistic view. Twenty-nineteen looks set, for some at least, to be the year subsidy-free solar becomes a reality. The impact of that reality on the secondary market is uncertain. There will almost certainly be more available assets in the coming years, but those backed by ROCs will retain their appeal over those whose returns are at the whim of the merchant market.

Investors in the UK market have ridden the peaks and troughs of activity just as much as the developers that have fuelled them over the course of the last five years but their paths look now more intertwined than ever. ■