(BN) Higher Interest Rates Pose Threat to $28 Billion Yieldco Market

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By Alex Longley

(Bloomberg) -- The yieldco market may face "a rush to the exit" from shareholders when interest rates go up.

Higher rates may spark a "vicious cycle" that limits the companies ability to acquire more assets, making them appear increasingly overvalued, Michael Liebreich, founder of Bloomberg New Energy Finance, wrote in a report Monday.

The so-called yieldco model is booming. Fifteen U.S. and European companies raised $12 billion in public markets over the past 30 months, and their market values have climbed 84 percent to almost $28 billion. The businesses offer dividends that make them popular with investors, especially when yields for government bonds are low. Rising interest rates would make government debt more competitive, a potential threat to yieldco share prices, and the U.S. Federal Reserve has indicated that rates may begin to climb this year.

"Higher interest rates would mean lower share prices for yieldcos, and this would make it a lot more difficult for them to raise new equity," Liebreich said in the report, which was co-authored by New Energy Finance Senior Analyst Angus McCrone.

Yieldcos currently pay annual dividends of 5 percent to 6 percent, which would be less competitive if U.S. 10-year rates return to their 2007 level of 5.3 percent Liebreich wrote.

Yieldcos are essentially holding companies for a portfolio of operating power plants. Developers always need capital for new projects, so they create a separate, publicly traded unit to buy the assets once they're completed. The yieldco's function is to collect revenue from selling electricity, helping fund the purchase of more power plants.

Yieldco IPOs

The six U.S. yieldcos that had initial public offerings in 2013 and 2014, including SunEdison Inc.'s TerraForm Power Inc., are up by about a quarter from their IPO prices, according to New Energy Finance.

New technologies may make these yieldcos more profitable, said Jeff McDermott, managing partner of Greentech Capital Advisors LLC.

"The next generation of technologies in wind and solar will lead to much lower costs of generating electricity, and thereby a massively larger addressable market," McDermott said by e-mail. "We continue to believe that yieldcos can reach $100 billion market capitalization."

The U.S.-listed companies tend to pay out more of their cash flow as dividends than European yieldcos. As a result, they tend to be seen as growth stocks in the U.S. and less risky in Europe.

European Model

"The model is very different in the U.S. in terms of how the asset base is being grown by the U.S. firms, the kind of finance mechanisms they are using," Mike Bonte-Friedheim, founding partner of

NextEnergy Capital, an investment adviser to the Guernsey-based yieldco NextEnergy Solar Fund Ltd., said by phone.

Yieldcos in Europe have encountered some speed bumps.
France-based Solairedirect SA postponed its planned 217 million- euro IPO ($239 million) in April because of a lack of interest, while Germany's Chorus Clean Energy AG put off its 125 million- euro IPO this month citing the Greek financial crisis.

While interest rates are a cloud on the horizon, Liebreich says the model has established itself as part of the renewable energy industry.

"The yieldco itself, however, meets a real need and is here to stay," he said in the report.

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