

# Alternative energy finance: The cold war

As energy prices in Europe soar with the approaching winter and trigger a political storm, BRAVE Partners looks at the factors driving this. The bottom line is that Europe needs energy independence and that requires investment in both new energy sources and in the infrastructure to diversify supply away from Russia.

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## Have I Got News for You

The seminal British TV comedy show "Have I Got News for You" sums up Europe's current dependence on Russian gas in the opening sequence. A Russian in a bearskin hat turns the valve on a pipeline and progressively the lights over Western Europe in the backdrop go out.

## Bear hug

The UK is somewhat isolated from the full impact of Russia driving energy pricing due to the North Sea resources. However the state of the North Sea is in many ways the story of European energy. The

Europe is currently dependent on Russia for one of its major energy sources – natural gas. The Russian pricing has little to do with supply and demand and a lot to do with a monopoly position – which it is seeking to further entrench. New and diverse energy sources are the only way out for Europe and that means investment.

previous energy crisis in Europe occurred in 1973 with the OPEC oil shock. The Arab members of OPEC, Egypt, Syria and Tunisia ceased to sell oil to the United States and her allies. This was in response to US policy in the Middle East, including support for Israel in the Yom Kippur war. In many ways the UK economy did not fully recover from the oil shock until oil production in the North Sea paid for the Thatcher economic transformation of the UK economy in the early 1980s. Oil boomed for decades, but in 2007 the UK again became a net importer of oil. It is thought that the need to import natural gas occurred a year earlier in 2006. Despite huge finds of natural gas in the North Sea, the UK is less self sufficient in gas than it is in oil. This is down to the domestic energy mix in the country.

## Jumping Jack Flash

As the lyrics from the Rolling Stones song go: "I'm Jumpin Jack Flash, it's a gas, gas, gas". In the UK energy went gas, gas, gas. Self-sufficient production and the difficulty in transport compared to oil made natural gas abundant and cheap compared with oil. Moreover, due to the extensive use of gas for cooking, much of the UK was on the mains gas supply. Households converted their heating rapidly from

coal, oil and electricity (in reality coal and oil as well at that time) to natural gas. Over time, cost and cleanliness has also shifted a lot of the UK electricity generation towards gas.

## Out of gas

The once abundant North Sea is now running out of natural gas. The UK is no longer self sufficient and is becoming increasingly reliant on imports through pipelines from Norway and The Netherlands. The UK and Norway are the largest oil and gas producers in Europe, so this situation worsens the further east you go in Europe, until you hit Russia where all the gas is found.

## Gas pricing in Europe

Now that the UK has to import gas it is exposed to global gas prices. As natural gas is a substitute for oil, its market price is linked to oil. Russia is particularly adamant on the oil price link for natural gas and so this system dominates pricing in Europe.

## East end boys and west end girls

Whilst gas is a substitute for oil, it is not a perfect substitute – ie it is not completely interchangeable. To fully utilise natural gas, a different infrastructure to oil is required. America shows this perfectly.

America shows that there is a supply and demand dynamic to natural gas that should make its pricing independent of the oil price. It is simply not in Russia's interests to accept that.

America is a huge importer of oil. On the flip side the significant progress that companies such as Chesapeake have made in drilling for shale gas has made America massively over supplied in natural gas, as it does not have the infrastructure to take advantage of this. America is subject to the global oil price, so its oil price is the same as it is in Europe. However, natural gas in the USA prices on supply and demand. As of October 20, NYMEX natural gas was at \$3.56/mmBtu, with UK natural gas at \$10.03/mmBtu – almost a 1:3 difference. This difference is driven by different supply and demand dynamics that exist because natural gas is not as easy to transport and store as oil.

## Supply and demand

Whilst demand for energy in the USA is huge this demand has always been met by oil and coal. An infrastructure for delivering natural gas simply has not developed. Friends of the BRAVE Partners who live on Long Island (and commute into Manhattan every day) are not on a gas main. In the UK this would be the equivalent of not having a gas main in St. Albans!

In 2010 gas consumption in the UK was 51,607 million tonnes of oil equivalent. The figure for the USA was 24,087,939 million cubic feet of gas which equates to 607 million tonnes of oil equivalent (nearly 90% less than in the UK).

## Grin and bear it

Norway and Russia have given some concessions on oil indexed pricing – Norway more than Russia – as oil indexed pricing rose to a 50% premium to the spot market. However, Russian firms – Gazprom in

particular – are seeking to lock in their dominance of European power prices by buying energy assets in Britain, Germany and across Europe. With the UK needing, by the Government's own estimations, £200bn invested in new electricity generation capacity, investment will be crucial – but the outcome might depend even more critically on who the investors are.

## Opportunity

BRAVE Partners believes that there is a significant investment opportunity in the European energy sector. This is both in technological development of new energy sources and in the infrastructure required to bring these energy sources on line.

Investors have the opportunity to make exceptional returns with the right projects and entrepreneurs have the opportunity to build major, world class businesses.

## BRAVE Partners services

BRAVE Partners is a boutique investment bank that specialises in the alternative energy and (re)insurance sectors. The firm is currently working on a number of transactions to finance energy assets and projects and has successfully secured an offer of over £60m of equity for a 50MW renewable energy project.

BRAVE Partners differentiates itself through the engineering knowledge and background within the partnership. The firm seeks to understand and present both the financial and the technology side of projects and technologies that are essential to the energy supply and security of the UK and Europe.

## Interaction

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- BRAVE Partners is a boutique investment bank with specific expertise in the alternative energy sector.
- The firm believes that a number of energy projects offer attractive rates of return that are sustainable in the long run due to pressures driving an increase in power costs.
- Many projects are capital intensive. Investments can be augmented in certain circumstances by capital attracted by tax advantages in well structured renewable projects.

### • BRAVE Partners can:

- Advise on investments in energy projects and assets.
- Advise management teams on developing investable business plans and find investment for projects.
- The firm has experience across a number of geographies and technologies.

### • BRAVE Partners has:

- A track record in successfully sourcing investment for energy projects.
- Recently obtained an offer of over £60m of funds for UK generation capacity.

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