A different world, a greener world?

Can private debt funds play a role in building a greener economy after COVID-19?

Craig Reeves
Founder
Prestige Funds

In July 2020, UK Chancellor Rishi Sunak unveiled a GBP 3 billion stimulus package as part of his Summer Economic Update to Parliament. This was targeted specifically at the UK's 'green' economy and was composed of a combination of grants, subsidies and loans. This included GBP 1 billion for a Public Energy Fund that is intended to decarbonise public sector buildings.

The UK, like other countries, is very focused on the reduction of greenhouse gas emissions, and sees this process as being one of key strategic importance. Chancellor Sunak's measures alone are hoped to slice UK greenhouse gas emissions by half a megaton while at the same time creating more than 140,000 new jobs in the sector.

The package demonstrates that the UK government recognises the important of re-greening the economy as part of the post COVID-19 recovery in the country. While government funding is going to play a critical part in this, private finance also has a role to play.

A different world, but will it be a greener world?

We will be emerging from the current pandemic into a very different world, but the climate challenge is one priority that will not have gone away. The fund management sector should have an important role to play at a time when there is more emphasis on ESG criteria in the way money is being managed by the industry. Indeed, next year will see an upgrade to MIFID2 rules where product providers and financial advisers will be required to demonstrate the 'sustainability' of an investment.

Investment into the private lending sector was one theme that had been expanding rapidly last year.[1] Within that, we are seeing more lending capital being allocated to important small scale clean energy projects. The UK is considered a leader in this area.[2] Beyond the advice to householders on how they can make their homes more energy efficient, there is going to be a bigger story around the ongoing development of critical green energy infrastructure, be it wind farms, solar farms, or biogas plants.

That use of the word 'farm' is apt, as it is the farming industry in the UK which has been taking the lead for many years now in the development of on-farm clean energy. This trend has occurred as farmers have been faced with rising electricity prices at a time when governments have also imposed higher taxes on landfill. Farmers have the advantage of space and, in many cases, ready sources of organic waste. While the presence

1 Financing SMEs and Entrepreneurs 2019, OECD Policy Highlights.

2 'UK renewables prove a shining success during pandemic', Financial Times, 17 May 2020

of marquee wind farm projects has generated considerable media interest, many farms have been diligently developing their own on-farm clean energy resources.

Biogas and anaerobic digestion

Biogas has come to the fore as a key component of on-farm energy. Biogas has the double utility of delivering sustainable energy while consuming organic farming waste and turning this into fertiliser. Biogas is not a new technology, but it is becoming more sophisticated and is in much wider use in the UK than historically.

Also called anaerobic digestion, the technology can be deployed as small, localised plants that can also generate sufficient surplus electricity to earn additional income when sold back into national grids.

Anaerobic Digestion (AD) is a proven technology which could deliver a staggering 30% of the UK's carbon budget in 2030, while also providing green heat to 6.4m homes.[3] During the pandemic lockdown in the UK, AD plants proved themselves to be extremely resilient, and all the operational plants funded by Prestige Funds remained fully functional. Prestige via its dedicated, specialist Finance Arranger has operated in this space for almost a decade.

If the UK is going to reach its government's 2050 target of net zero emissions, this technology has an important role to play. The potential carbon savings are massive. According to ADBA (the Anaerobic Digestion & Bioresources Association), at its full potential, AD provides emissions savings equivalent to the emissions of all the HGVs currently operating on British roads.

Financing of biogas on a national level requires considerable expertise, especially when focusing private capital in the important ESG role of funding green energy infrastructure. In effect, private lending in this space mirrors the important higher level financing the UK government is carrying out, but at a more localised level.

Specialist private lending funds have the advantage of the local networks and expertise required to manage large loan books within the agricultural and clean energy brackets within the UK.
This is not something achieved overnight.

UK agricultural sector has remained robust during lockdown

SMEs within the agricultural sector also have the advantage of having continued to function at close to or at maximum capacity as food demands within the UK have not lessened during lockdown. Many agricultural businesses face challenges as a consequence of COVID-19, but these are rarely down to a lack of demand.

Making these businesses more productive and more energy efficient, essentially more robust, is

3 *Biomethane:* The Pathway To 2030 (ADBA research report, 2020)

part of the role of commercial lenders like private debt funds. There is an important social role to be played here, as these SMEs have faced a dearth of borrowing options as big banks have pulled out of the sector post-Great Financial Crisis.

Now we have another crisis on our hands, and it remains important for private debt funds to remain fully engaged with smaller businesses and advise them on how they can capitalise on the shift to a greener energy infrastructure and the benefits that can accrue from this.

This means playing a far more consultative role than simply assessing credit risks and carrying out initial on site visits. Technical expertise is required to help farmers and other rural SMEs to implement biogas or other clean energy generating facilities. Ongoing support and advice may be needed to ensure such plants are both meeting the needs of the farms they serve, while potentially also generating further wattage for local communities.

Conclusion

Local energy projects are going to be essential if the UK and other countries shift post COVID-19 towards a greener economy. Financing such infrastructure is not the role of governments alone, many of which have been stretched with the need to support economies through the coronavirus crisis. But what we do have here is an opportunity to create new jobs within the energy industry, many of them within local communities. Small scale projects are already proving that they can replace electricity being generated with fossil fuels.

Over the next two decades we anticipate that private lending funds will play a very important role in financing the expansion of clean energy infrastructure in the UK and further afield. More importantly, they have a role to play in the effective deployment of capital to SMEs in the immediate aftermath of the pandemic. There is an opportunity here to accelerate the transition to a greener economy through the effective use of private investment within the lending sector.

Prestige Funds

Alternative Fixed Income Opportunities

Prestige Asset Management Limited

36 Spital Square, London, E1 6DY, United Kingdom

T: +44 (0) 203 178 4055
F: +44 (0) 203 004 9690
E: info@prestigefunds.com
www.prestigeassetmanagement.co.uk
www.prestigefunds.com

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