Unlocking clean energy with next-gen investment tech

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The amount of project finance capital going into renewables has steadily increased over the past five years. Specifically, renewables has grown to just below 30% of project finance transactions closed in 2021 and such deals accounted for 60% of total volume (295 deals).[1] This good news, however, could easily lead to complacency that project finance is on the right path, and that deal flow is sufficient to help meet ambitious goals such as the Paris Agreement, limiting global temperature rise this century to under 1.5 degrees celsius above pre-industrial levels and helping countries better deal with the impact of global warming. In fact, to accelerate further investment in renewable and low emission energy, the project finance industry must adopt modern investment technology and up level its data management practices now.

Global energy consumption rising

One-third of global emissions are associated with fuels used to generate electricity, and global electricity consumption is expected to triple by 2050. In order to meet this demand and reduce our emissions footprint, we must expedite investments into renewables and low-emissions technologies. The unavoidable reality is that many, many more Project Finance deals are needed to meet the challenge of climate change. To put the urgency of the task in further perspective, the 1.5°C Paris Scenario will require investments of USD 5.7 trillion per year until 2030, and this will require the redirection of USD 700 billion in annual investments in fossil fuels towards energy transition technologies. Multilateral agreements and governments can encourage this investment via policy, but markets and greater innovation will be crucial to success.

Current limits to project finance

It is, however, easier said than done to shift capital toward much needed investments. The significant average size of oil and gas projects (circa $3 billion) vs renewable energy ($200m)[1] puts a potential cap on the total number of fundable projects. The reason why: there's an inherent challenge at the heart of originating, closing and managing all complex, high expertise, long-term projects. It can take just as much time and effort to develop, close and manage smaller projects as it does larger investments, and this means while there are many renewable projects ready to go, the current cost of capital is geared toward larger deals. Incentives, as a result, are misaligned to drive the substantially greater volume of renewable and low emission project finance deals required to meet our goals.

Here is where modern investment technology and, in particular, improved data management can provide the project finance industry the support it needs. To understand how, it's worth a deeper dive into what makes project finance different from other asset classes.

First, each deal is like a snowflake, unique in nature, and as such, each deal demands an individual approach, building custom models and analytics. Second, data comes from different directions and in a variety of formats. It is neither digitized nor standardized. Third, such deal characteristics make workflows slow and manual, particularly when compared to other asset classes. This has meant the only way for financial advisors,arrangers, sponsors and investors to take on more deals is to add staff—generally not a feasible choice given the current cost of capital for smaller renewable projects.

Unlocking crucial capital

As a result of the current limitations of project finance, innovation has been difficult, and progress has been stymied due to the lack of technology platforms sophisticated enough to adapt to the nuances of project finance, such as the disparate sources of data. Fortunately, that is no longer the case, and the industry now has the opportunity to embrace a scalable, centralized source of truth solution designed to meet the unique needs of project finance.

A modern project finance solution will bring much needed standardization, yet still allow for flexibility to tailor a deal to a project's needs. It will establish new data pipes to connect the funding ecosystem—from developer to lead arranger to investor.

A virtuous cycle

In sum, if we wish to meet our climate change goals and expedite essential investment in renewable energy sources and lower-emissions fuels, we must modernize the project finance investment and data infrastructure with scalable solutions, and we must do it today. The result will be a virtuous cycle as more funds flow into renewables and low emission projects, reducing the cost of smaller deals and further increasing funding.

[1] Based on *IJGlobal's* 2021 transaction data for primary issuance project finance transactions closed.

