

Part I – Three Truths About the Renewable Energy Revolution

The 55 megawatt geothermal power station in northern California had become so run down during its 14-year shut down that bankruptcy was the only way out. And there the idle facility sat, month after month, with its steam wells sealed, despite the fact that oil prices were soaring to record highs. The wells were finally drilled open in the spring of 2005, when U.S. Renewables Group (USRG), a company organized to acquire, develop and operate renewable energy and clean-fuel assets, performed due diligence in advance of a possible asset acquisition.

The steam beneath the ground was strong and plentiful, and USRG purchased and refurbished the Bottle Rock geothermal plant. The financials proved positive and rewarding almost immediately: less than a year after closing the deal, USRG sold a 50 percent stake in Bottle Rock to The Carlyle Group; and, over the next decade, USRG stands to gain a considerable sum in tax credits for spearheading this renewable energy transaction.

Buying Bottle Rock will enable USRG to provide relatively inexpensive and clean electricity to thousands of California households. But the agreement also underscores the new realities of the 21st century energy industry, which increasingly is becoming the *renewable* energy industry. There are three truths underlying this sweeping market transformation:

- Renewable Energy Is Imperative – We live in a carbon-constrained world, so we must find ways to produce new megawatts of energy without injecting fresh doses of CO₂ into the atmosphere. This is a massive and unprecedented problem that requires governments and global capital markets to collaborate in the kind of unparalleled public-private partnership advocated by Jeffrey Garten, Dean of the Yale School of Management. That's why it's encouraging that 21 states, representing 40 percent of the U.S. population, have adopted Renewable Portfolio Standards (RPS) that mandate new – and renewable – ways to generate power. In the end, though, it will fall to the private sector to develop structural and lasting solutions to this crisis; we cannot expect \$100 gas rebates from Congress to clean up the environment. The focus will be on renewable energy (RE), which represents just 6 percent of the U.S. electricity market today but is the fastest growing segment in the industry with annual expansion of 10-20 percent. This buoyant growth should continue for at least the next decade because nuclear power has perceived

environmental and security risks, natural gas capacity has been curbed due to the excessive build-out and price increases of recent years, and coal presents emission issues. RE should also prosper because of increasing global demand for clean fuels like ethanol and bio-diesel, challenges that are straining U.S. refinery capacity, and the need for a domestic supply hedge given the perils and uncertainties of the world's oil and gas markets.

- Renewable Energy Is Profitable – Renewable energy assets are profitable and increasingly cost competitive with fossil fuels. The high price of gas and oil has contributed to this new financial equation, but RE tends to have low or zero fuel costs and relatively low operating costs. RE has also benefited greatly from technology advances that have lowered capital costs and increased reliability in the last decade.
- Renewable Energy Is the Future – The RPS laws in 21 states are expected to result in the development of nearly 50,000 megawatts of new renewable energy production capacity by 2017. Delivering this additional RE for electricity will require between \$10 billion and \$20 billion of much-needed equity capital.

Part II – Exploring, Enhancing and Extracting Renewable Energy Value

There is significant – and growing – demand for renewable energy and clean fuels, but until USRG was formed in 2003, no major investor was willing to fully explore the market and take meaningful and muscular equity positions in these assets.

That has changed dramatically over the past three years; during this time, USRG has raised close to \$500,000 in investment capital and assembled, acquired and managed an impressive portfolio of RE and clean-fuel assets. In addition to purchasing Bottle Rock, USRG now owns and operates three landfill methane facilities in Los Angeles and San Antonio, and is backing and building three plants in the Midwest that will produce 300 million gallons of ethanol per year in partnership with Cargill and other institutional investors.

USRG is a unique and vertical RE player. With a team of 10 seasoned and specialized deal makers, project managers and operators, the firm makes its RE and clean-fuel investments where equity capital is scarce and technology risks are low. Then it deploys a cadre of veteran engineers and contractors to enhance value by rebuilding and running the asset. If it's renewable power from steam, wind, sun, biomass or landfill methane, USRG extracts value by making and selling electrons at a profit; if it's renewable fuel, the firm manufactures and marks up the ethanol or bio-diesel. In both cases, the assets appreciate and there is a reduction in carbon emissions.

Until USRG's formation three years ago, one of the most pronounced and profound problems in RE and clean-fuel investing was connecting the fledgling venture capital-backed technologies in the field with the power of the global capital markets, which have the ability to finance broad acceptance and adoption of innovation. USRG builds bridges between the venture and capital markets – between Sand Hill Road and Wall Street – by taking pre-commercial renewable energy or clean-fuel projects and making them scalable and reliable enough for regulatory

compliance and bank financing. As part of this linkage, USRG has joined forces with Rustic Canyon Partners, a venture capital firm with more than \$800 million under management.

Part III – Conservative Investing in Renewable Energy

Investing in renewable energy or clean-fuel projects with USRG is analogous to investing in real estate. In return for a capital injection, the investor obtains ownership of a tangible asset, receives current income, and benefits from the asset's long-term capital appreciation.

There are also a number of innovative back-end exit strategies that can help investors capture and monetize the increased value USRG creates with each project. Consider, for example, the financial power of a REIT-like structure based on the bundled value of the biggest geothermal facilities in the United States, or an IPO for a large-scale, state-of-the-art ethanol plant.

Renewable energy or clean-fuel investing is new and cutting-edge, but it should never be confused with the faddish Internet mania of the late 1990's, with its extraordinarily inflated valuations and massive price spikes. In fact, RE investing is truly conservative. The growth of electricity capacity is expected to track at about 1-2 percent a year, and the megawatts that are added must be clean in order to preserve the atmosphere. Unlike the volatile and unpredictable dotcoms, RE investments over time can be expected to generate unlevered returns in the 15 percent range and levered returns that approach 25 percent.

For its part, USRG seeks increasing returns, but never at the expense of increasing the intensity of carbon emissions. USRG knows the sky has limits; the unrealistic Internet entrepreneurs of the past thought the sky was the limit.

Part IV – The Next Wave of Renewable Energy Investing

Renewable energy and clean-fuel investing are steadily evolving. Right now, for example, USRG has one fund for U.S.-based RE projects, but based on expected demand and the anticipated energy environment, there could soon be a hedge fund for RE, a tax-focused RE fund, and a foreign RE project fund.

The global appetite for renewable energy and clean fuel is evident. In China, for instance, provincial governors have been instructed by Beijing to limit carbon emissions. One province south of Shanghai the size of California can only run its factories four days a week because of a lack of clean electricity. Renewable energy solutions must be found to compensate for the 25,000 megawatt shortfall.

Going forward, renewable energy experts and investors will try to uncover bargains by taking advantage of mispriced BTU values. Getting paid to remove medical waste and then heating and gasifying it into a lucrative renewable energy source is just one of the new frontiers awaiting discovery and large-scale commercialization.

Time is being compressed and moving fast in the RE industry – because it has to. Nobody knows just how damaged the atmosphere is from carbon emissions, but nobody wants to choke off the heavens for a single day. Renewable energy helps lessen this potential stranglehold on the environment. The principals at USRG know this, as well as the fact that there are trillions of dollars to be made investing in RE and clean-fuel assets; the good news is that a growing number

of profit-driven investors around the world are beginning to share this belief – and not a moment too soon.

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