Results analysis: Octopus Renewables Infrastructure

ORIT continues to grow its dividend in step with inflation...

Update

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- **Octopus Renewables Infrastructure's (ORIT) annual results to 31/12/2024 show a NAV total return of +2.5% (2023: +2.1%). At an operational level, ORIT's power generation grew by 7%, revenues by 12% and EBITDA by 16%.**

- **ORIT met its dividend target of 6.02p, 1.24x covered by operating portfolio cash flows. The dividend saw an increase of 4% over 2023, in line with UK CPI for a third consecutive year. The target dividend for the year ending 31/12/2025 is, similarly, an increase in line with UK CPI of 2.5% to 6.17p and is expected to be fully covered. At the current share price (as at 31/03/2025) the yield is c. 9.4%.**

- **The NAV per share was 102.6p (2023: 106.0p), a c. 3% decline. The main components of the slight fall were small adjustments in the development pipeline, some lower than forecast payments to recently completed assets and some shortfalls in financial and technical performance in some projects. Overall though, these were relatively minor adjustments.**

- **ORIT's weighted average discount rate was stable, falling from 7.2% to 7.0% largely through construction premiums falling away as assets became operational. ORIT's discount rate is calculated on operational assets, and factoring in the developer company assets as well as impacts of FX and the RCF, the expected portfolio return is 8.1%.**

- **Fixed revenues rose from 81% to 84% (forward fixed for two years), reducing ORIT's exposure to short-term power price fluctuations. In addition, 48% of revenues are inflation-linked over 10 years.**

- **ORIT was geared 45% LTV at the end of the period (or 82% as a percentage of NAV). Post year end a new debt facility was secured against some of the UK assets, reducing the size of the more expensive revolving credit facility to £150m (resulting in a c. £850k annual saving) and bringing the average borrowing costs down from c. 6.5% to 5.25%. The capital allocation policy, below, sets out the long-term goal for gearing.**

- **ORIT defines itself as an impact fund with a core impact objective of accelerating the transition to net zero through its investments and is classified under Article 9 of SFDR. The impact highlight from the financial year is 1,240 GWh renewable energy generated (2023: 1,161 GWh), with the portfolio having the potential to avoid 383k tCO2 . A detailed breakdown including the cumulative impact over five years is in the annual report.**

- **Capital allocation strategy.**
  - **ORIT currently trades at a c. 37% discount, and in response the ORIT board has set out a capital allocation policy.**
  - **During the year ORIT announced a £10m share buyback programme, and at 25/03/2025 had executed £8.7m of this. €7m was invested in a further funding round for developer Simply Blue, with ORIT owning 20%. A Swedish wind farm was sold for €74m, delivering an 11.3% IRR over the life of the investment. As a result of this sale, total proceeds from capital recycling reached £161m.**

- **Post-year end ORIT set out three clear capital allocation goals, first extending the share buyback programme by a further £20m, second a target to reduce gearing below 40% LTV by the end of 2025, and third a commitment to further asset sales of at least £80m by the end of 2025.**

- **ORIT will continue to make selected value accretive investments, assessed against the relative benefits of buybacks and debt reduction.**

- **Chair Phil Austin said: ""During FY 2024, and to date, we have continued our disciplined approach to capital allocation, reducing debt, buying back shares, executing on strategic asset sales and making targeted investments where we see opportunity for future value creation. We are steadfast in our commitment to delivering value for shareholders, and the Board, alongside Octopus Energy Generation, is actively evaluating enhanced strategic initiatives to unlock further growth."**

Kepler View

At an operational level this was a solid set of results, with positive earnings growth from the operational portfolio. Further, **Octopus Renewables Infrastructure (ORIT)** has made good progress on reducing the size and cost of debt which ultimately could feed through to further dividend growth. Clearly ORIT faces the same macro headwinds as the rest of its peer group, with investors still reassessing the damaging investment trust cost disclosure debacle and trying to navigate the ups and downs of the bond market, which competes for their attention. But while clearly the US is taking a different approach to renewables, the jurisdictions ORIT operates within all remain firmly committed to renewable energy. Further, ORIT's sale of the Swedish wind asset, for an IRR of over 11% from construction to sale shows that it is much more than a bond proxy, with equity upside potential. On top of this, 2025 is set to be the fourth consecutive year of dividend growth in line with inflation.

While macro factors are beyond the control of ORIT's manager, the capital allocation policy is its practical response to some of the challenges. Any capital allocation policy needs to balance the competing factors of gearing, share price and the need to support the portfolio. One of ORIT's key strengths in our view is its investments in developers and construction assets, which require much lower initial capital than purchasing operational assets. This is illustrated by ORIT's ability to stand its ground in the 2024 funding round for Irish developer Simply Blue, with a €7m investment well within its resources despite not being able to tap the equity markets for further capital (due to the discount). This size of investment, which also comes at a much higher potential IRR than an operational purchase, can be balanced against the goals of reducing debt and buying shares back, both of which ORIT has achieved in a balanced manner.

One of the other key features of ORIT is that it provides diversification across geography (i.e. weather system and political jurisdiction), technology (solar, onshore and offshore wind, energy storage) and stage (i.e. operational, development and construction). The annual report shows an analysis of the quantitative benefit of diversification. The full explanation of this is beyond the scope of this short note and we will expand on it in a forthcoming full note on ORIT. The essential concept is that the diversification provides higher certainty over electricity generation output and lower volatility of returns than a similar set of assets not diversified by technology and geography. Intuitively investors probably already knew this, but it's interesting to see the results of a detailed simulation of this and, as we say, we will explore this further in a longer note.

Overall, with a stable NAV that has been validated by several disposals in the last 18 months, positive operational progress resulting in a progressive and covered dividend and a balanced capital allocation policy, we think ORIT's 36% discount looks notably unjustified.

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