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# Results analysis: SDCL Energy Efficiency Income

**SEIT reaffirms dividend target and updates on plans to address the discount...**

Update
**10 December 2024**

- **SDCL Energy Efficiency Income (SEIT) has reported its interim results to 30/09/2024, with the NAV stable at 90.6p (31/03/2024: 90.5p) and aggregate dividends of 3.16p compared to 3.12p for the same period last year. SEIT made a profit before tax of £35 million (2023 equivalent period: Loss of £89m).**

- **At the current share price, SEIT yields c. 11%. First half dividends were covered 1.1x by cash and the board reaffirmed its dividend guidance for the year ending 31/03/2025 of 6.32p (2024: 6.24p).**

- **SEIT's portfolio valuation was £1,103m compared to £1,117m at 31/03/2023, with the main difference being the sale of UU Solar for £90m in May 2024.**

- **The weighted average discount rate of 9.4% (leveraged) is in line with the previous two from 31/03/2024 and 30/09/2023, although various small adjustments were made up and down on specific assets.**

- **SEIT's gearing was 35% LTV, with 11% at a fund level through the trust's revolving credit facility (RCF) and 24% at a project level. The same figures calculated as a percentage of NAV were 54%, split 17% at the trust level and 37% at a project level. The average interest rate was 5.6% and the average remaining life 4.1 years. Over 80% of debt at a project level is amortising, meaning it will naturally run off over time.**

- **SEIT's discount at the half year end was c. 30% and is currently c. 36% .The Morningstar Renewable Energy Infrastructure peer group average was c. 20% and is currently c. 28%. The board and manager set out a plan to address the discount in the final results to 31/03/2024 and provide an update and expand on this in the interim results, detailed in the next section.**

- **Investment of c. £98 million into organic investments and existing commitments during the period (30/09/2023: £93m). The plan detailed below provides information on the minimum return threshold required for new investments.**

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- **Tony Roper, chair, said: "We are pleased that both SEEIT's operational and financial performance for the period were in line, or a little above budget and generated cash flows that fully underpinned the Company's progressive dividend policy. We are strongly of the view that SEEIT's share price does not reflect the value of its investments nor the cashflows derived from them. To this end, the Board and Manager remain focused on addressing the share price discount by supporting the marketability and liquidity of the Company's shares."**

## Kepler View

In the weeks before **SDCL Energy Efficiency Income's (SEIT)** results announcement, the Morningstar Renewable Energy Infrastructure peer group in which it sits experienced significant discount widening,

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seemingly a result of the US election and investor worries about the different approach the new administration is expected to take to renewable energy. Share prices of other renewable energy companies were similarly hit.

While it's quite likely in our view that this is a sector-wide over-reaction, SEIT has some specific differences in its business model compared to the peer group. First, the vast majority of SEIT's revenues do not rely on any form of subsidy or incentive, and its projects are primarily rooted in their commercial attractions. In essence, SEIT provides its corporate customers with ways to save money through a combination of more efficient use of energy and more efficiently delivered energy, for example eliminating transmission losses by locating power generation close to where it is consumed. Second, SEIT has very limited merchant exposure, with most of its long-term revenues contracted, and low direct exposure to power prices. SEIT is really an equity investor in platforms that provide corporate customers with efficiency solutions, so it participates not only in the contracted revenues that come from these solutions, but in the growth of the platforms themselves. Third, SEIT's project-level debt is mostly amortising and so is repaid over a period of time. Many of SEIT's assets and investments extend well beyond the life of the debt, giving the trust different options in the future to enhance earnings. The team also point out that one of the first moves the new US administration made was the formation of a new Department of Government Efficiency, so 'efficiency' appears to be a positive theme in the US, which SDCL counts as its single largest country exposure at 67%.

Given, though, the c. 36% discount SEIT trades at, the manager and board set out an update on the plan to address the discount, the main points being:

- Disposals. In May, SEIT sold portfolio holding UU Solar for £90m, a 4.5% premium to the prevailing valuation. A process to sell stakes or to invite co-investment in Onyx and EVN have begun with first round bids expected soon, with the team targeting completion in the first half of 2025. Proceeds from disposals will be allocated to the repayment of the RCF and share buybacks will also be considered.

- Focus on NAV return. The team highlights that holdings Onyx and EVN are growing fast and Onyx is also ahead of its deployment targets. Onyx, which provides on-site generated solar power to commercial and industrial sectors across 14 US states, continues to create and convert significant pipeline through its development activity. The trust continues to fund Onyx's development pipeline which is expected to be NAV accretive.

- Capital Allocation. Any new investments must be attractive when compared to the returns generated by share buybacks. For example, at the year end, the return generated by share buybacks would be 13% and this would effectively be the minimum threshold return for any new investment, including funding the growth of existing investments.

- Reducing short-term borrowings. The sale proceeds noted above were to reduce the RCF to below £100 million and future disposals will be used for the same. The RCF has been used to fund organic investments and at 30/09/2024 was £165m (or 11% LTV). The objective is to reduce the short-term RCF to £100-150 million during the second half of the calendar year 2025. Additionally, some short-term debt may be shifted to longer-term amortising project debt matched to the individual project.

Without getting into the flamboyant rhetoric, it is fair to say that the incoming US administration has an agenda much less focused on 'energy transition' and whatever the practical realities that unfold over the next few years, this is a negative for investor sentiment right now. We think SEIT's business model, while aligned with energy transition, is relevant to customers with concerns about energy security, either more locally due to extreme weather events, or more widely due to geopolitical instability, as well as more straightforwardly simply helping customers to reduce costs. Thus, in our view, SEIT's business model doesn't really align with the main negatives of investor sentiment, and as the board's plan to address the discount unfolds, the current discount could prove to be a significant opportunity.

**Click here to read the HY report on RNS**

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