US Cleantech Investment Climbs 41% in 2Q2008 to Nearly US$1 Billion – the Highest Quarter on Record

Ernst & Young LLP

Venture capital investments in US cleantech companies grew by 41% to US$961.7 million in 2Q2008, up from US$683.5 million in 1Q2008, according to an Ernst & Young report based on data from Dow Jones VentureOne. This is the highest total cleantech investment on record, and comes amidst a quarter in which overall venture capital investment was down by nearly 8%. Year-on-year cleantech investment follows this upward trend, increasing 83% from 2Q2007.

Energy/electricity generation companies attracted the most investment of any sector this quarter with US$494.9 million – 52% of the total. The top three deals of the quarter were solar-related companies. The deals included, SunEdison, in Beltsville, MD, which raised US$131 million, eSolar, in Pasadena, CA, which raised US$130 million and BrightSource in Oakland, CA, which raised US$115 million. It is also worth noting that corporate investors were involved in all of these deals.

Energy efficiency companies made up 20% of total investment dollars and continue to be a top cleantech investment segment despite a slight 4% decline to US$188.3 million in 2Q2008. The third largest segment this quarter was alternative fuels, which comprised 13% of the overall US cleantech market. The segment, made up entirely of biofuels transactions, attracted US$129 million of investment, down 44% from the previous quarter.

"Efficiency-related investments, such as smart meters and LED technologies, have seen relatively steady levels of deals and investment over the past few quarters because they can be ready for an exit more quickly than other renewable energy technologies," says Joseph A Muscat, Americas director of cleantech and venture capital, Ernst & Young LLP. "Investment in increased efficiency can have a shorter payback period since many of these technologies are relatively capital efficient compared to the capital intensity of a manufacturing-heavy segment like biofuels."

Deal volumes in 2008 were distributed across the stage of investments, which is noteworthy given that the majority of deals in 2007 were seed and first round transactions. Also, while overall cleantech investment rose 41%, the number of deals increased by only one to 41 deals in 2Q2008 compared to the preceding quarter. Later stage deals accounted for 39% of the transactions in 2Q2008.

Market Drivers

The price of energy is driving demand for cleantech innovation in the corporate sector, particularly with the average price of oil increasing 98% from June 2007 to June 2008 – from US$67.49 to US$133.88 – according to the Department of Energy (DOE). Additionally, global energy demand is slated to increase 57% from 2004 to 2030, according to the DOE. In response, investors and corporations alike are setting long-term cleantech investment strategies.

New corporate commitments to climate change are also stimulating cleantech activity. Seventy-seven percent of large corporations have integrated cleantech into their internal systems or supply chains and 63% offer cleantech-related products, according to a recent Ernst & Young survey of 150 large corporations. Large industrial, oil, automotive and utilities corporations are increasingly entering strategic partnerships and making acquisitions to find alternatives to oil. According to John S Herold Inc, Shell invested US$1 billion over the past five years in renewable technologies and Chevron publicly committed to invest US$100 million per year. DuPont and Genencor, a division of Danisco A/S, announced a commitment of US$140 million over the next three years as part of a joint venture to develop solutions for the production of cellulosic ethanol. These long-term commitments and investments suggest solid, continued growth in the sector.

Cleantech deals were responsive to activity in the capital markets. During the first half of 2008, there were 115 M&A alternative energy transactions globally. The 44 that reported acquisition values raised US$7.2 billion, according to John S Herold Inc. The largest US deal was done by private equity firm ArcLight Capital, which acquired the Tehachapi wind farm project in Kern County, CA from Australian investment group, Allco

Finance, for US$325 million. Another notable US corporate example is Duke Energy's US$240 million acquisition of Catamount Energy, a Vermont-based wind power company from Diamond Castle Holdings. Overall, 46% of the M&A transactions were done by private equity firms and 54% were corporate deals.

Additionally, three of the ten US-domiciled IPOs in 2Q2008 were cleantech companies and accounted for US$1.7 billion of the US$3.9 billion raised (44%), according to Thomson Financial's SDC. The largest cleantech IPO was American Water Works, based in Voorhees, NJ, which raised over US$1.2 billion.

It is now the largest publicly owned water and wastewater utility company in the US. This IPO underscores the increasing interest by investors in water as a segment of cleantech, a trend that is expected to continue. Looking forward, the IPO pipeline includes seven cleantech-related companies, two of which are venture-backed. Two of these companies are looking to raise over US$300 million, including Noble Environmental Power – a Connecticut based wind company – which is expected to raise around US$375 million.

"In a challenging market, investment in the cleantech sector remains strong because these companies provide cross-sector solutions to economic and environmental challenges," explained Muscat.

Note to Readers:

Ernst & Young uses the following definitions to classify the cleantech industry and its sub-sectors:

Clean technology encompasses a diverse range of innovative products and services that optimise the use of natural resources or reduce the negative environmental impact of their use while creating value by lowering costs, improving efficiency, or providing superior performance.

- Alternative Fuels – Biofuels; natural gas (LNG)
- Energy/Electricity Generation – Gasification, tidal/wave, hydrogen, geothermal, solar, wind, hydro
- Energy Storage – Batteries, fuel cells, flywheels
- Energy Efficiency – Energy efficiency products, power and efficiency management services, industrial products
- Water – Treatment processes, conservation & monitoring
- Environment – Air, recycling, waste
- Industry Focused Products and Services – Agriculture, construction, transportation, materials, consumer products

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