ENERGY PRIORITIES™
Smart Energy Information & Ideas for Business

What do VCs Look for in Clean Energy Companies?

SEATTLE -- One of the highlights of today's "Investing in Clean Energy for the Pacific Northwest" is the panel of venture capitalists. The GP panel is a Who's Who of energy VCs. What attracted them to energy? Is it to make money, or to save the environment? What sets casual funds apart from serious players? How do strategic investors and public policy affect investments?

Denis Du Bois
October 04, 2006

Clean energy is attractive because there are so many sectors in the industry, says Technology Partners' Ira Ehrenpreis. It's relatively underserved by VCs, compared to life sciences and IT. Martin Tobias of Ignition Partners agrees that it was getting challenging to make money in the more efficient IT market, so he looked for something more lucrative. He found it in Imperium Renewables (which operates Seattle Biodiesel), where he is Chairman and CEO.

Energy venture capital fund general partners panel at the Stoel Rives conference on clean energy investing. From left: Nancy Floyd, Ira Ehrenpreis, Martin Tobias, Chuck McDermott, Kirk Washington and John Rockwell. (EP photo)

Kirk Washington of Yaletown Ventures saw opportunities to incrementally improve the incumbents' ability to compete with newcomer alternatives. The solar sector, for example, needs a way to address the shortage of silicon, and engine manufacturers are increasingly challenged to meet emissions standards.

Energy efficiency is not a big enough pain point for customers at the moment, says DFJ Element's John Rockwell, but mandates and incentives will drive up interest. Meanwhile, load shifting and demand response technologies have his attention.

Chuck McDermott of Rockport Capital expects changing electric rate structures to increase interest in efficiency. Moderator Nancy Floyd of Nth Power agrees that a tariff reflecting the true cost of energy would be a catalyst for good VC returns in the efficiency and peak load management sectors.

"Producing high-quality financial returns is one of the best things we can do for the environment."
--Ira Ehrenpreis, Technology Partners.

Ehrenpreis observes that casual funds invest in solar if they want just two or three clean-tech investments in their portfolios. Other areas take expertise. Kirk Washington adds that the sector is incredibly fragmented, and each investment requires research into the "tiny crevices." He worries that, with an influx of investors to clean tech, enthusiasm will replace due diligence.

Most of the panelists agree that corporate LPs are important. McDermott notes that Coca Cola and Wal-Mart facilities are large enough that they can create critical mass for a new technology. Rockwell says corporate partners help them understand pain points and opportunities in the market.

Corporate LPs are as important in energy as in IT, says Ehrenpreis, the difference is the diversity of the market. In the energy sector, investors don't just need to understand the inner workings of Fortune 500 CIOs, they need to learn about each new sector.

There are two kinds of corporate investors, according to Tobias. The "good kind" are those companies who will be consumers of his biodiesel. The "bad kind" are vertically integrated companies looking to squeeze the profitability out of the refining process.

Non-financial returns are of little importance to most LPs, so they aren't at the top of the list for VCs. Kirk Washington says environmental benefits come third after cost and efficiency metrics.

"Producing high-quality financial returns is one of the best things we can do for the environment," says Ehrenpreis. "That will create growth and opportunity for companies who are making a difference."

Public policy factors into investment decisions, but Tobias is the only panelist who admits to influencing it. He says his company spent considerable time and money to support the passage of a renewable fuels standard in their home state.

"The impact of policy is absolutely huge, there's no way to ignore it," says McDermott. If subsidies disappeared, he's afraid returns would disappear with them. (Clean Edge analyst Ron Pernick later clarified that there are no subsidy-free sectors in the energy industry; even the extremely profitable petroleum industry has taxpayer supports.)

Kirk Washington adds that each company should have a person who keeps their eye on government activity. Ehrenpreis is watching for opportunities in green trading, driven by policy decisions in California and follow-on states.

"The biggest misconception in clean tech is that the price of oil drives value for the whole sector," says Ehrenpreis. "Not a single panelists here, with the exception of Martin, would change their investment decisions if the price of oil dropped."

The GP panel was part of a full-day conference entitled "Investing in Clean Energy for the Pacific Northwest" presented by Stoel Rives, Nth Power and Northwest Energy Angels.