

# **ENERGY INFRASTRUCTURE INVESTMENTS THE ROLE OF PRIVATE EQUITY**

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*Steve Herman*  
*Managing Director*  
*Energy Capital Partners*

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# Energy Capital Partners Overview

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## ➤ **Well capitalized with focused investment strategy**

- \$2.25 billion private equity fund
- Investing in energy infrastructure
  - Generation, transmission, renewables, storage, pipelines
  - Focused on North America (New Jersey & California offices)

## ➤ **Experienced team of energy professionals**

- Multi-disciplinary team
- Significant industry experience

## ➤ **Initial Transaction—FirstLight Power Resources**

- Acquired from Northeast Utilities 1440 MWs of generation in NEPOOL Market for \$1.3 billion
  - MA & CT hydroelectric fleet
  - MT Tom coal-fired facility
- Curt Morgan CEO; headquartered in Hartford, CT

# Energy Private Equity Primer

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- Definition of Private Equity
- Private Equity Growth
- Energy Industry Capital Needs
- Investment Process Overview
- Recent Private Equity Transactions
- Near-Term Opportunities

# Definition of Private Equity

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## ➤ **No precise definition of private equity funds**

- *A broad term referring to managed pools of capital raised from private sources*
- *Some private equity funds invest across a broad spectrum of industries (e.g., KKR, TPG, Blackstone) while other funds focus on particular industries (e.g. technology, healthcare, energy)*

## ➤ **Compared to hedge funds**

- *Short-term trading focused using swaps, arbitrage, derivatives and leverage tools*
- *Hedge funds have moved into asset investments via distressed debt*

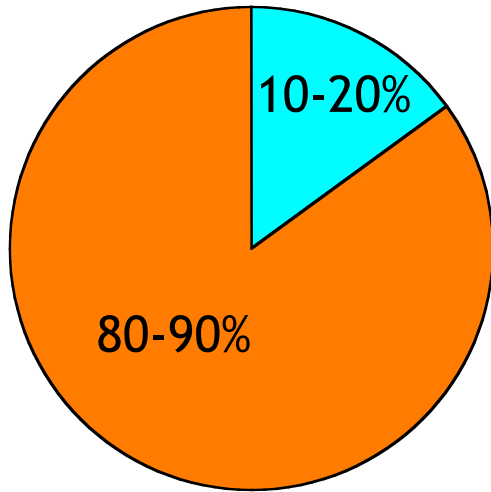
## ➤ **Compared to venture capital**

- *Venture capital invests in early stage start-up enterprises*
- *Private equity focuses on more mature opportunities*

# **Growth in Private Equity**

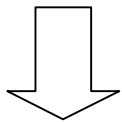
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# Significant Pension Fund Reallocation

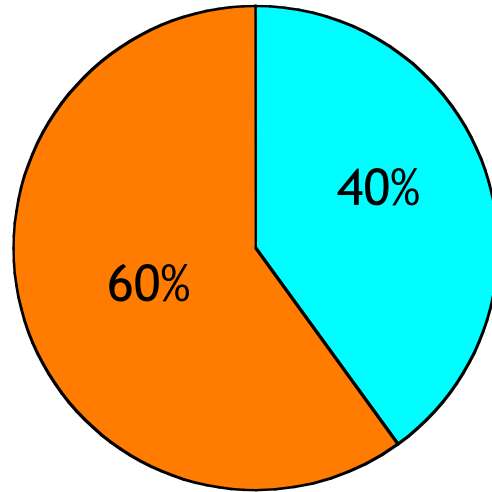


■ Alternatives ■ Public Equity and Fixed Income

Traditional

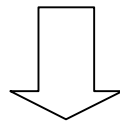


**Expected Portfolio  
Return  $\approx$  8%**

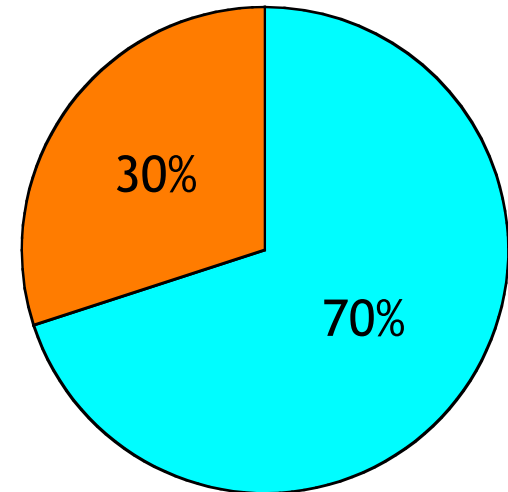


■ Alternatives ■ Public Equity and Fixed Income

Conservative  
Reallocation

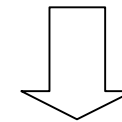


**Expected Portfolio  
Return  $\approx$  9%**



■ Alternatives ■ Public Equity and Fixed Income

Aggressive  
Reallocation



**Expected Portfolio  
Return  $\approx$  12%**

## Five Year Return Performance

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	<b>Multi-Year Return</b>	
	<u>Annualized Return</u>	<u>Alternatives %</u>
Stanford	12%	50%
Yale	17%	66%
Harvard	18%	70%

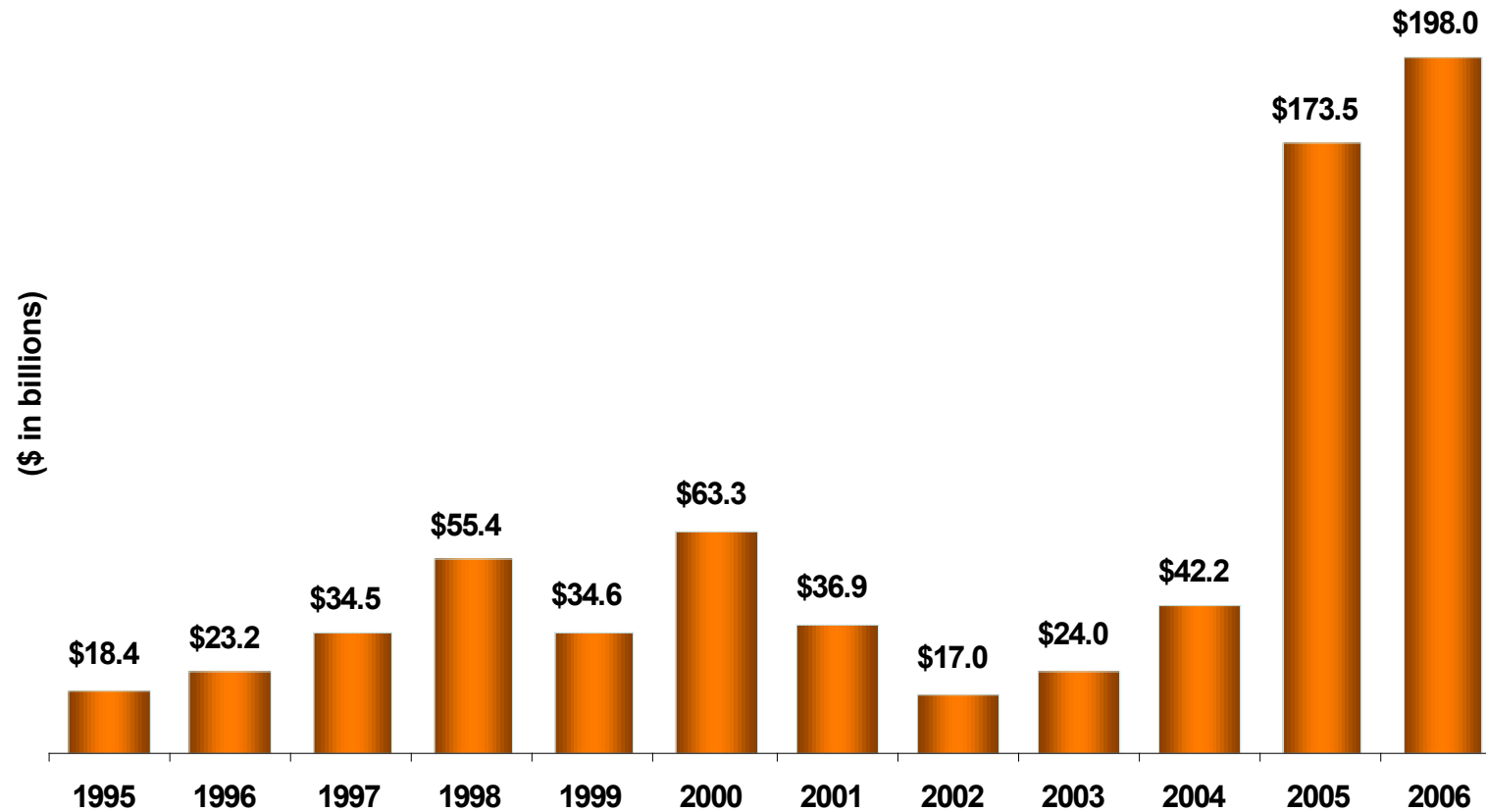
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# Dramatic Growth in Private Equity Funds

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## Capital Raised by U.S. Buyout Firms

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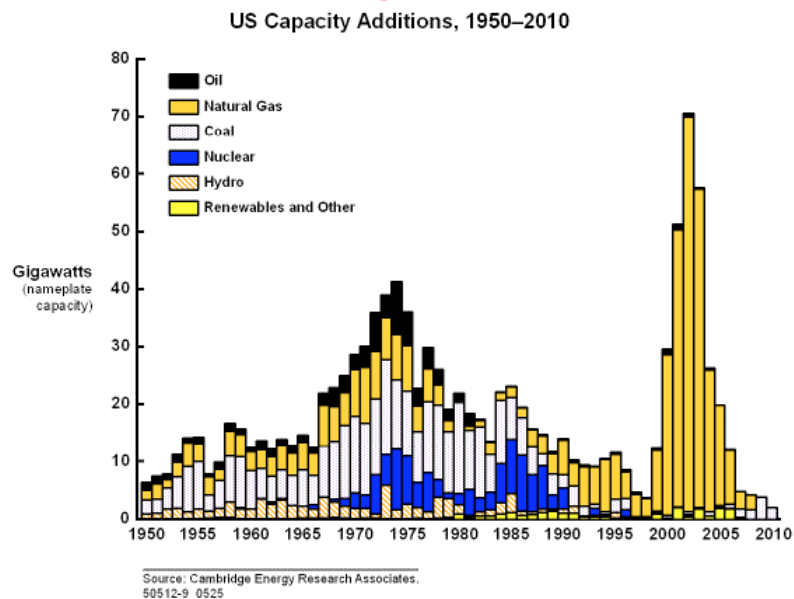


Source: Buyouts

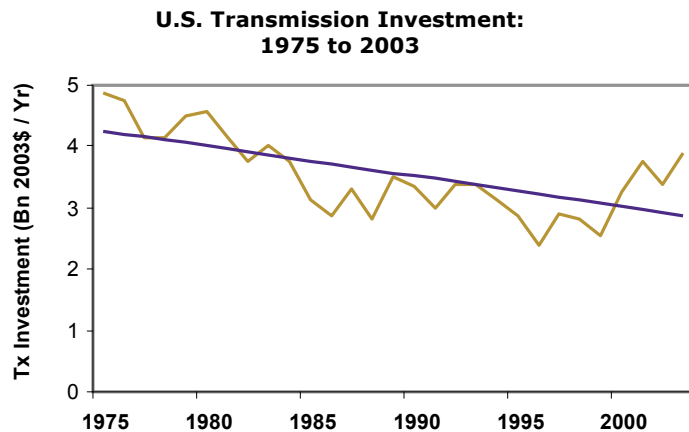
# **Energy Industry Capital Needs**

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# Capital Needs and Historic Trends



- **CERA estimates the U.S. power sector will need about \$800 billion of capital investment by 2020--**
  - \$275 Bn for new power plants
  - \$50 Bn for environmental retrofits
  - \$150 Bn for new transmission
  - \$300 Bn for electric distribution
  - \$25 Bn for conservation and efficiency (DSM)



- **The current net book value of the U.S. power sector is approximately \$700 billion**

# **Private Equity -- Investment Process Overview**

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# Investment Process Overview

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## ➤ **Transaction Sourcing**

- Relationships
- Open-door initiatives
- Fund initiatives
- Competitive sales

## ➤ **Investment Section**

- Return
- Risk assessment

## ➤ **Due Diligence**

- Management team
- Quality of asset

## ➤ **Value Creation**

- Expansions and efficiency improvements
- Commercial optimization
- Opportunity for improved capital structure
- Synergies via mergers and roll-ups

# **Power Private Equity: Investment Opportunities**

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# Private Equity Energy Players

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Fund	Size	Power Strategy
<b>GENERALIST</b>		
Blackstone	\$20 billion	- Mega deals
KKR	\$16 billion	- Mega deals
Texas Pacific Group	\$15 billion	- Mega deals
Madison Dearborn	\$6.5 billion	- Generation, renewables
<b>SECTOR FOCUSED</b>		
ArcLight	\$2.1 billion	- Contracted generation
EIF	\$1.0 billion	- Generation, renewables, transmission
Energy Capital	\$2.3 billion	- Generation, renewables, transmission
First Reserve	\$7.7 billion	- Oilfield services, coal, generation, midstream
LS Power	\$1.5 billion*	- Generation, renewables, transmission
Riverstone	\$4.5 billion	- Energy-focused (midstream & E&P); generation, renewables
Tenaska	\$0.8 billion*	- Generation
<b>INFRASTRUCTURE</b>		
Macquarie	--	- Utility

\* Raising a new fund

## Energy Trends Impacting the Industry

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- Strong electric and gas demand growth
- Reserve margins tightening
- Impending need for new-build decisions
- Shortage of traditional capital sources
- Chronic underinvestment in the grid
- Persistent energy commodity price volatility
- Renewable energy development boom
- Growing GHG concerns and carbon controls
- Regulatory risk for utility mergers
- Strong acquisition and development deal flow

# Power Generation Transaction Landscape

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## Revitalized Interest in Merchant

- Successful large portfolio sales: NU, Constellation, Mirant, DENA, Encana
- Highly competitive bidding for coal-fired, new CCGT and gas storage
- Higher volume of single asset transactions

## Significant Amount Of MW Changing Hands

- Successful merchant sales and leverage finance markets have motivated strategic sellers
- Availability of commodity hedges provides significant leverage capacity

## Regional Generation Market Recovery

- The market continues to recover from the overbuild of 2000-2003
- Certain regions are anticipated to have oversupply past 2010 while others are already at or near acceptable reserve margins

## Financial Sponsors Are Taking the Lead

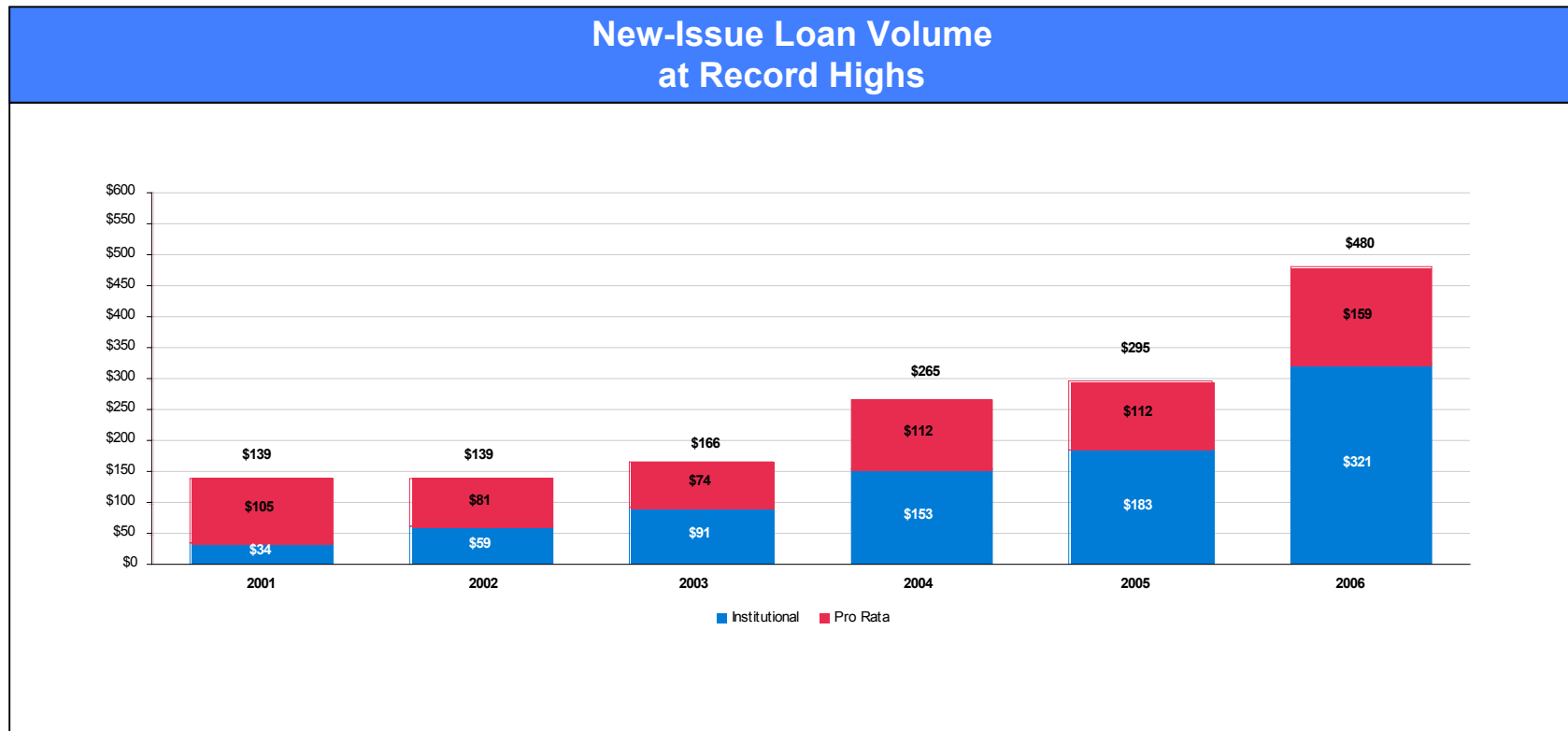
- Access to capital in the leverage finance markets continues to play a pivotal role in energy infrastructure transactions
- Hedge funds willing to invest across the entire capital structure

## Financing Activity in the Power Sector

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- **We have seen an unprecedented level of leveraged financing activity in the power sector over the last 18 - 24 months.**
- **The execution market of choice has been the Term Loan B market**
  - Filled the financing void left after the merchant power crisis in the early 2000s
- **Term Loan B market provided significant capacity and situation-specific flexibility**
  - Less restrictive covenants; minimal prepayment penalties
  - Able to find demand and price points all the way down the credit spectrum
  - Investors consist of CDO / CLOs, insurance companies, hedge funds and, to a lesser extent, commercial banks
- **Recent deal flow has been driven by:**
  - Stapled financings,
  - Construction projects, and
  - Recapitalization of formerly distressed power projects
- **Pricing levels remain close to historic lows**
  - For example, B1 / B+ is approximately 225 bps over LIBOR

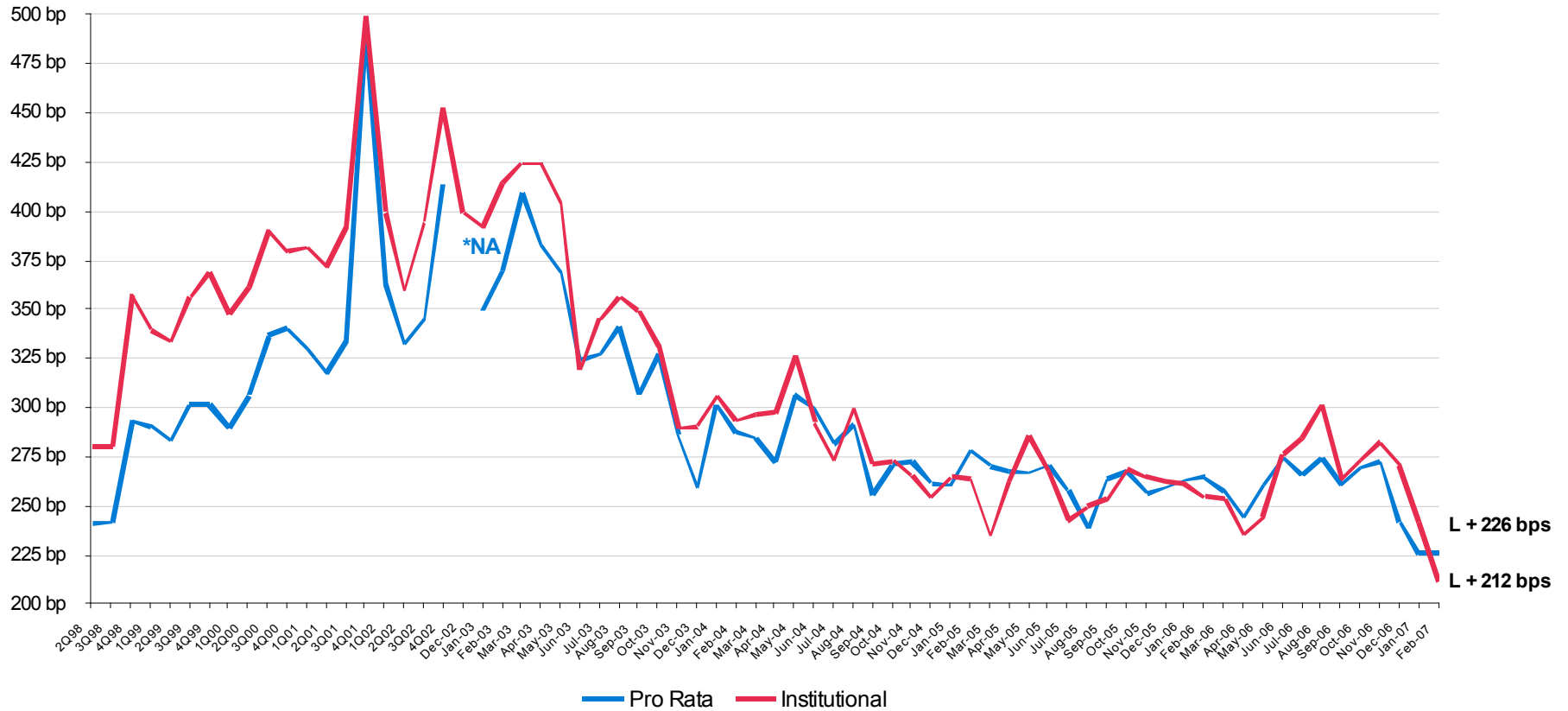
# 2006 Was A Record Year In the Leveraged Loan Market



Source: S&P / Portfolio Management Data.

**After setting new records in 2006, the Leveraged Loan Market is beginning 2007 with healthy conditions.**

# B+ / B Syndicated Loan Pricing



Source: S&P/Portfolio Management Data.

\* Not enough deals to form a meaningful average.

## Selected Large Transactions

Target	Acquiror	Size	Comments
Encana (Storage)	Riverstone	\$1.5 billion	<ul style="list-style-type: none"> <li>- Acquisition of multiple gas storage assets</li> <li>- U.S. and Canada footprint</li> </ul>
TXU	KKR, TPG, Goldman Sachs; Citigroup, Lehman, Morgan Stanley	\$44 billion	<ul style="list-style-type: none"> <li>- Take-private / LBO</li> <li>- Separating of utility, genco (18,000 MW), and energy business</li> <li>- Carbon strategy, 5-year hold</li> </ul>
NU (Generation)	Energy Capital	\$1.3 billion	<ul style="list-style-type: none"> <li>- Acquisition of 1440 MW, primarily hydro / pump storage</li> <li>- Establishes platform in New England</li> </ul>
Astoria / Boston Generating	NA	\$5.2 billion	<ul style="list-style-type: none"> <li>- Private merger of genco portfolio companies held by private equity / hedge funds</li> <li>- Creates 5,000 MW scale in NYC and Boston load pockets</li> </ul>
LS Power	Dynegy	\$3.7 billion	<ul style="list-style-type: none"> <li>- Public/Private merger of genco portfolios in MW, NE and West</li> <li>- Combined 20,000 MW fleet</li> <li>- Includes development joint venture</li> </ul>
Longview	First Reserve	\$1.8 billion* * Cost to construct	<ul style="list-style-type: none"> <li>- Development/Construction--PJM coal plant</li> <li>- Four-year time horizon</li> </ul>

# **Near Term Opportunities**

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# Private Equity and Project Development

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## ➤ **Source of Funding**

- Development expenses
- Project equity

## ➤ **Credibility with Counterparties**

- EPC vendors
- Lenders
- Fuel suppliers

## ➤ **Complementary Skills**

- Revenue / hedging strategies
- Financing optimization

# Private Equity and Asset Acquisitions

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## ➤ **Asset sale / divestiture drivers**

- Revised business strategy
- Book income / accounting limitations
- Shortage of capital
- Monetization of asset ownership

## ➤ **Private equity advantages**

- Focused on cash returns, not on book income or quarterly results
- Accelerate development / expansion opportunities
- Efficient use of hedging
- Emphasis on value creation
- Financial structure optimization