

Capital Power

September 04, 2024
01:15 PM EDT

Fedja Saric: Good afternoon, folks, and welcome to the Barclays CEO Power and Energy Conference. My name is Fedja Saric and I'm part of the Barclays investment banking group for energy transition. I'd like to introduce our next company and speaker. Capital Power Corp. is one of Canada's largest independent power producers, at 9.2GW of generating capacity, about equally split between the United States and Canada. Our speaker today is president and CEO, Avik Dey. Prior to joining Capital Power in 2023, Avik spent two decades in a variety of energy roles, leadership, operational, and investing. Ladies and gentlemen, Avik Dey.

Avik Dey: Thank you. It's an honor to be here, and I'm excited to talk about Capital Power and share our story with you. Look, there's lots we can talk about in the power space, so I would love to keep this informal and have a conversation. And I'll probably go off the podium here because that's just going to be easier.

For 20 years, we looked out at the forecast for power markets in North America, and we looked at a mature market. We looked at a market that was driving efficiency, energy efficiency, and over time, was flat, to a declining power demand market. And that's all changed. Now for Capital Power, we are focused on building the leading North American power producer. We were focused on that last year. We were focused on that in 2015. We were focused on that in 2010. But what that meant for us as a company over the course of the last 15 years of our existence was we were focused on providing reliable, affordable and clean electricity. What did that mean? That meant our focusing on gas-fired power generation. Today, we are the only North American public company, the only one, that operates on both sides of the border, Canada and the US, and has consistently continued to acquire natural gas-fired power generation. We're the only public company that's continued to expand, operate, build new gas-fired power generation capacity. So today, we're for the first time in 25 years, we're now looking out at a secular growth opportunity in terms of power demand. We are perfectly situated to go do that on behalf of our shareholders, in partnership with long-term commercial off takers, and in partnership with stakeholders, whether they're load-serving entities, utilities, utility commissions, RTOs. And that's why we're excited about our company today.

So, a little bit about our company. We have 9300MW of capacity. We're the fifth-largest gas IPP in the US, largest in Canada. We have- our business is simple. We have three core businesses. Only three core businesses. First one, flexible generation. 80% of our capacity, 7800MW, is gas-fired. Half of it in Canada, half of it in the US. That is the biggest part of our business. It's what we do well, and it's what we, I would say, are well-positioned to deliver in North America.

Second business is renewables. So we've been a renewable developer for 15 years. We've got 1.5GW of operating capacity, we've got a two gig pipeline, across solar and wind. And importantly, when you couple that with our flexible generation business, it puts us in a very unique position to deliver solutions for commercial off takers. Included in that is also our battery storage business, which we've got two active projects in development in Ontario.

The third piece of our business is trading and origination. This is a critical part of what we do. So we operate in our four core markets today, Alberta and Ontario in Canada, and

[WEC] and MISO in the US. The Alberta power market is a merchant market. It's an energy-only market. To be able to operate in an energy-only market, you need to be able to trade. And that has been a core competency of ours for the last 15 years. We know how to contract, we know how to hedge, we know how to trade gas-powered environmental credits. And when you combine these three businesses together, it allows us to provide reliable, affordable electricity to the markets we serve and to commercial customers. And so when we when we look at that spread, why we're excited about our business today, everyone talks about data centers and what that's going to mean for the market. And I'm happy to go into detail there. But what's more important than focusing exclusively on data centers, there's multiple reasons why electricity demand growth is growing over the next 20 years. Between now and 2030, power generation demand in the US is going to double, and that's not just because of data centers. It's because of reshoring, industrial reshoring, it's because of continuing electrification, it's because of GDP growth and it's because of data centers. And so for us, being diversified across markets in North America, we are well-positioned to service those companies that need utility-scale power generation. And we are well-positioned against our peers who are IPPs because most of our peers have said "we don't buy gas. We have a gas-fired generation." And guess what? Today, the best way of providing reliable and affordable electricity is through gas-fired generation. And so for our capacity and fleet to be able to come into those large wholesale customers and say, "let us work with you, let us provide reliable generation through gas-fired power generation, let us work to decarbonize that with renewables and battery storage projects, and let us wrap that and marry that with our trading and origination capabilities as your partner," is an incredibly compelling offering.

Now, why does that make buying Capital Power attractive? Well, if we talked about electricity demand any time in the last 20 years, we would have looked at this chart and the dashed lines announced today and the timeline, call it, the last 25 years. You know, between 2010 and now, that's been marked by the energy transition phase. Renewables have gone from 1% to 14%, and overall U.S. supply was growing. Now underlying that, that blue line, is firm power supply. Well, firm power supply was declining slightly over time, so if we looked at this at any point in time in the last 20 years, pulled it from the IEA, we would have seen coal-fired power plants retiring, gas-fired power plants retiring, and that being displaced at 2 to 1, 3 to 1 of renewable capacity. So the top line is what we all focused on. The blue line is what we didn't focus on. What our company saw and what RTOs saw, what ISO saw, what utility commissions saw, is that for the better part of last 20 years, firm power demand meeting firm power supply. We had cushion. And that's the spread between that mustard line and the blue line. It was never an issue. It wasn't a concern, that we were going to figure out distributed generation, and people were going to have at-home batteries, we were going to do community solar. And the reliance on grid wasn't critical. So, reliable generation wasn't at risk. Well, as we rolled forward through the pandemic to today, that curve has tightened. So before I could spell data center and if we were having this conversation a year ago, I would have said this is a secular generational investment opportunity. Why? Because the tale of critical reliable gas generation assets was being heavily discounted, because the more renewables we added to a grid, the more you needed reliable power. And the fact that we traded away this arb and those curves, those bottom two curves converged, we had this great opportunity to create real value, generate cash flow, positive NPV in terms of, you know, capital investment into existing capacity. And that's what our company has done. Since 2016, we've acquired six plants, each and every plant that we bought gas-fired, we were able to upgrade, expand, re-contract and improve the economics of them. Every single one. It was because of this.

Now, we've entered what we're calling energy expansion because demand is growing. And guess what? That top gray line is still up and to the right. Why? Because everyone's building out renewable capacity. But, those two bottom lines have crossed. Firm power demand is growing, and it's higher than what firm power supply is providing, which is why we now have a bottleneck and why we haven't seen a slew of PPAs for Gen AI hyperscale data centers, because this is what we now have to go solve. It's not just about we and a counterparty signing and executing a PPA. You have to work with the load serving entity, you have to understand transmission distribution bottlenecks, you have to understand what's going into rate base or not, and be able to solve that puzzle. And that's what we're excited about in our business, because we believe we're well-positioned to go deliver that.

Here, we just show, you know, the doubling of power demand. Gen AI - everyone has seen this page. I think how I think about the gen AI opportunity is I think it's going to come in phases. You know, I think the hockey stick projections around data center demand is going to be in multiple phases. The first phase is going to be that 20 to 30GW that gets built out, to actually go build out the capacity of the LLMs. But then after that, the growth is going to come through business use cases. How many of us are signing up for ChatGPT licenses? Yeah, I'm overstating that a little bit, because the business use cases are significantly beyond that, but that initial wave is going to happen, and that arms race to build out that capacity is well underway.

When we talk about data center meeting firm demand, so in order to meet the same capacity as a 1000 megawatt gas plant, you would need 10x the capital, 9x the capacity, so 9000MW of renewables, and a thousand times land to provide the same reliability that a 1000 megawatt CapEx- 1000 megawatt plant would require. Right? That is astronomical, the spread. So again, what this brings the conversation back to is how do we find reliable power and then augment with ancillary renewables to drive down carbon footprint, and optimize transmission distribution? So, how does this play into our strategy?

I told you about the three businesses that we have - flexible generation, renewables, trading and origination, and where the growth opportunity for us is, is in each of those. But the one that we're most excited about is that fourth box, which is balanced energy solutions to commercial customers. Now, we're talking about it in the context of a data center, but it could equally be a petrochemicals plant or an agriculture firm, or a plastics firm, or an energy refinery. Anyone that has a large demand for power on site, we believe, will increasingly have to go find their own power solutions, because grids can't take down that capacity and provide grid support or grid back up to them, because ratepayers won't have it. You know, if any of us look at our utility bills, 50% to 75% of our utility bill is the rate base, it's not actual generation. Well, that's what's come home to roost now. And so this is where we as a company are spending our time. It's identifying on our own fleet those opportunities to expand, providing reliable, affordable electricity, by doing the things we've been doing for 15 years - operating, expanding, re-contracting. And then demonstrating to wholesale customers why we can be their partner of choice, because we can provide that reliable power through flexible generation. We can build renewable capacity for them to generate credits for them, and we can manage energy risk on their behalf as a counterparty. And so this is where this dovetails into that fourth business line, balanced energy solutions. You know, the first two segments, flex gen and renewables, is actually building, managing, and operating the physical generation. And then the second and third, you know, we- 65% of PPAs in renewables in the US over the last 15 years are held by tech companies. They're procuring the power and being a counterparty on those renewables, to procure the credit, not the electricity. It's in jurisdictions they don't need the power. Well, those have been a critical element of growing renewable penetration in the US, from 1% to 15%- plus. It's been the major catalyst to building up this capacity. But today, going forward, that will not be the solution, because you need to have the generation where you have the load demand, and this is where we want to focus.

One of the things that's been a cornerstone of our success over the last 15 years is we've been exceptionally good at buying and optimizing gas-fired power generation. On average, we've achieved 6% to 9% accretion on an AFFO per share for each and every gas-fired power plant that we've bought. How we've done that is we have a perfect track record of operating, expanding, and recontracting and improving the economics of plants that we've bought. And so we continue to see that opportunity, in particular, now that we're looking at load growth and increasing reliability gaps in most of the markets we're in.

In terms of markets that we're in and the ones that we want to grow in, I described earlier four markets that we focus on in Canada - Alberta and Ontario. In the U.S., MISO and WEC. The characteristics that are familiar in each and every one of these markets is they're dependent on thermal for baseload generation, one. Two, heavy incentives around renewables. And three, the ability to contract with commercial offtakers. Those three ingredients are markets we thrive in, because the underlying volatility of higher renewable penetration, reliance on thermal, and ability to contract is where we generate alpha. Markets we'd like to grow in, or that we're open to grow in, are PJM and [inter-cost].

And so maybe I will end on this one, as we maybe open it up to Q&A, but we have a long track record, ten years, of delivering increasing dividends, consistent shareholder returns. We have a strong balance sheet, being investment grade that has been underpinned by this disciplined focus on providing reliable, affordable generation, and focusing our greenfield efforts around renewable development. And that underpinning of strong cash flow and managing energy risk against a contracted set of assets, and the merchant market in Alberta is what's underpinned the strong position that we're in. And so as we look long-term, we have been a strong dividend and growth story. We expect to continue that dividend growth in the future, and we're committed to delivering, you know, 12 to 14%, equity returns to our shareholders through a very well-defined and articulated, and what's been consistent, capital allocation approach to flexible generation, renewables, and trading.

So with that, we've got eight minutes left and I'm happy to take questions or have the conversation. I think we need to wait for the mike.

Unidentified Audience Member: Thank you. Looks like there's a chance to do some contracting at Genesee in terms of data centers. Recently submitted a bid today, so on that, can you talk a little more about that?

Avik Dey: Yeah, it's- we talked about it at our quarterly earnings call. We're excited about Alberta as a jurisdiction for data centers. I think when you look at Alberta as a jurisdiction, because it's an energy-only market, and it's open to new investment because we have existing capacity on transmission and distribution, to facilitate new load, because of the climate in Alberta, and the coolness of the weather there, the net heating and air conditioning cost is lower than other places, because of the strong gas supply and relative cost of that gas supply, you know, the province is incredibly well-positioned to take advantage of the data center opportunity. I think when we talked about this a year ago, naturally, the hyperscalers were looking for capacity in markets they were already in, not because the customers were there, but if you think about the front end or this first phase of data center buildout, as it relates to the LLMs, it's all proprietary, it's all [prop book] investment, right? It's not predicated on who the customers are for that LLM build up. So naturally, they looked at where they could do it near a place that they already had existing capacity. Well, the more time that passes from, you know, when they wanted that capacity to when interconnects will allow them to build it here, then you open and widen the aperture on markets and you look at a broader screening criteria. And this is where Alberta has become more and more interesting today than it was a year ago. So, because of those market factors, you know, when you talk to the end customer, you know, the customers that own that computing capacity, a year ago, number one was probably speed to market. And number two was "here's the five places we want that capacity." Well, speed to market is still number one. And number two is, you know, split down the list and everything else is, you know, expansion capability, proximity to fiber, energy costs, you know, timing of expansion, and flexibility of expansion. And most importantly, as we've learned, stakeholder support of that new capacity coming in. We have that in Alberta. We have a premiere, a minister of energy, a minister of utilities, a minister of technology, who are all very public in their support for bringing this industry in Alberta. Why? Because Alberta, 70% of our load is commercial off takers. The province knows how to work with industrial capacity. And so this is why Alberta is very exciting. We think Genesee is well-positioned. We're not in a position to say where we are in that process, but we're very excited about the opportunity. And you know, look, a number of things have to come together before we can solidify a commercial offering there, but we think it's incredibly well-positioned, and it makes very logical sense to build out data center capacity to serve hyper data centers in Alberta.

Unidentified Audience Member: [inaudible]

Avik Dey: So we're 900 people. We've got, roughly, 350 operating staff. We've got an engineering and operations team mostly headquartered out of Alberta that support that. But importantly, if you look at the IPP space, we do all of the engineering, all the sustaining and maintenance CapEx programs, all of that's done in-house across our fleet. It's one of our key comparative advantages. In total, we've got about 900 FTEs across the company.

Unidentified Audience Member: [inaudible] be part of the power corp, or the holdco, or what's your history?

Avik Dey:

The company's history? So Capital Power was spun off of Edmonton Power, EPCOR, which is a 150 year old utility headquartered out of Edmonton, Canada. And after deregulation, which occurred early 2000s, EPCOR decided to spin off all of the generation assets in 2009. So the company has been in existence 15 years, but it's born of a 150 year pedigree.

Well, good. Well thank you. Thank you for your attention, and appreciate your interest in Capital Power.