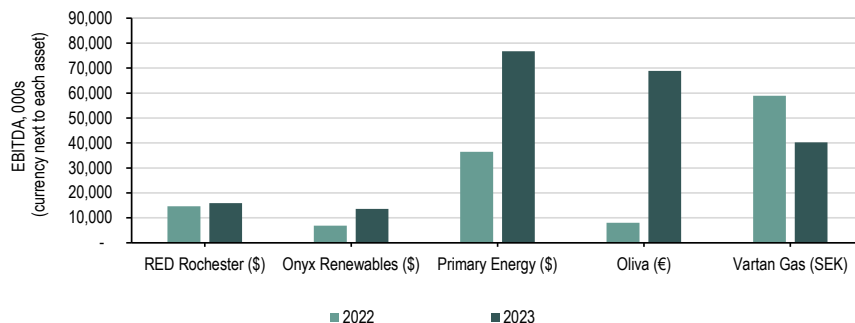


SDCL Energy Efficiency Income Trust

A deep dive into key assets

SDCL Energy Efficiency Income Trust (SEEIT) currently trades at a significant 46% discount to net asset value (NAV). This discount to NAV is larger than that of the company's wider peer group, which stands at c 34% (weighted average of 19 peers), and its 13% dividend yield is the second highest in the AIC Renewable Energy Infrastructure sector. SEEIT is possibly misunderstood as it has a unique mandate (energy efficiency) and a diverse set of assets, which make comparison to peers difficult. In this note we take a closer look at its five key assets, which made up c 75% of its gross asset value at 30 September 2024. Its assets are diversified by technology and are focused almost entirely on delivering energy efficiency as a decentralised service behind the meter, rather than supplying energy to the broader grid. Both features are arguably deserving of a premium, rather than a discount valuation compared to peers.

Historical EBITDA performance of assets



Source: SEEIT, Edison Investment Research

Unique within the sector

SEEIT's discount to NAV is the sixth largest of its relative peer group and is an outlier, among its sector peers, for a trust of its size. Renewable energy has struggled with investor perceptions for a range of reasons, including fluctuating merchant power prices and long-dated cash flows in a discount rate environment, yet SEEIT is actually less deserving of these generalisations. Its assets produce contracted revenues and profits, which are directly linked to counterparties/customers, and are largely unaffected by fluctuations in merchant power prices. SEEIT also has a relatively low level of gearing in comparison to peers, at 35% (as a percentage of enterprise value).

In this note we outline SEEIT's key assets and their revenue models, and include relevant data disclosed by the trust. The diversity in the assets' activities is wide: converting waste heat to energy at major US steel-makers, supplying efficient power to a local business park in the US, generating localised solar power in Europe and the US, biomass to energy in the olive oil industry in Spain and distribution of biogas in Sweden. SEEIT's c13% dividend yield was 1.1x covered in H124, and it retains growth options within its asset base, which are not reliant on economic subsidies.

Investment companies
Renewable energy infrastructure

22 April 2025

Price	46.45p
Market cap	£504m
Total assets	£1,102m
NAV	91.7p
Discount to NAV	49.0%
Current yield	13.6%
Shares in issue	1,085.4m
Code/ISIN	SEIT/GB00BGHVZM47
Primary exchange	LSE
AIC sector	Renewable Energy Infrastructure
52-week high/low	69.1p 43.6p

Fund objective

SDCL Energy Efficiency Income Trust's objective is to generate an attractive total return for investors, comprising a stable dividend income and capital preservation, with the opportunity for capital growth.

Bull points

- SEEIT provides a high dividend yield while trading at a significant discount to NAV, offering a total-return focus and an attractive entry position.
- A progressive dividend, which has been significantly covered since inception.
- Further scope for operation and efficiency gains within its portfolio, adding accretive value.

Bear points

- Coming out of a prolonged period of high inflation and interest rates, but there is still uncertainty within the economic and geopolitical environment.
- Counterparty risk (although SEEIT is well diversified).
- Investor sentiment regarding renewable energy infrastructure investment trusts remains relatively negative.

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Primary Energy

Introduction to Primary Energy – asset video



Source: SEEIT

Primary Energy had an equity value of c \$255m (15% of the total portfolio) at H125 (30 September 2024), up from c \$240m at FY24 and c \$241 at FY23, with \$160m in project-level debt. The business operates a portfolio of industrial energy efficiency assets, primarily serving major US steel producers through waste heat recovery and co-generation facilities. The company's core operations centre on energy recycling and efficiency projects at steel manufacturing facilities, with assets including Cokenergy and North Lake. These facilities are strategically crucial, converting waste gases from blast furnaces into electricity (North Lake) and utilising waste heat from the exhaust of coke ovens (Cokenergy), while significantly reducing CO₂ and SO₂ emissions. The operations are integral to its clients' environmental compliance and energy efficiency initiatives.

Revenue structure and historical performance (at 30 June 2024, regarding CY23)

FY23 EBITDA reached \$36.8m, showing modest growth from \$36.5m in FY22. The revenue model is predominantly based on long-term power purchase agreements (PPAs) with strong counterparties. The revenue contributions are structured as follows:

- Cokenergy constitutes the largest revenue stream with 54% of the total, converting waste heat to power and steam to sell to Cleveland-Cliffs' blast furnace #7 through long-term PPAs that are index-linked. These revenues are protected against demand fluctuations through a true-up mechanism.
- North Lake contributes 19% of revenue, through similar waste gas conversion operations and long-term protected PPAs as Cokenergy.
- PCI, 50% owned by Cleveland-Cliffs, generates c 7% of revenue, with revenues being demand-based. The asset pulverises metallurgical coal injected into Indiana Harbor Blast Furnace #7 for steel production.
- Portside revenues are capacity-based and represent c 18% of total revenue, and are generated through the sale of heat, power and softened water through long-term PPAs with United States Steel Corporation.
- Renewable energy credits (RECs) represent the final 2% of revenue.

Contract security and counterparty analysis

The business benefits from robust counterparty relationships with Cleveland-Cliffs and US Steel. A significant development in FY24 was the 12-year contract extension with Cleveland-Cliffs for the Cokenergy project, which enhances long-term revenue visibility. The majority of revenue is derived from services to Cleveland-Cliffs' blast furnace

operations at Indiana Harbor works.

Revenue protection mechanisms

The revenue model incorporates substantial downside protection through index-linked PPAs and true-up mechanisms for key assets, including Cokenergy and North Lake. This structure provides resilience against demand fluctuations, while Portside’s capacity-based revenue model offers additional stability.

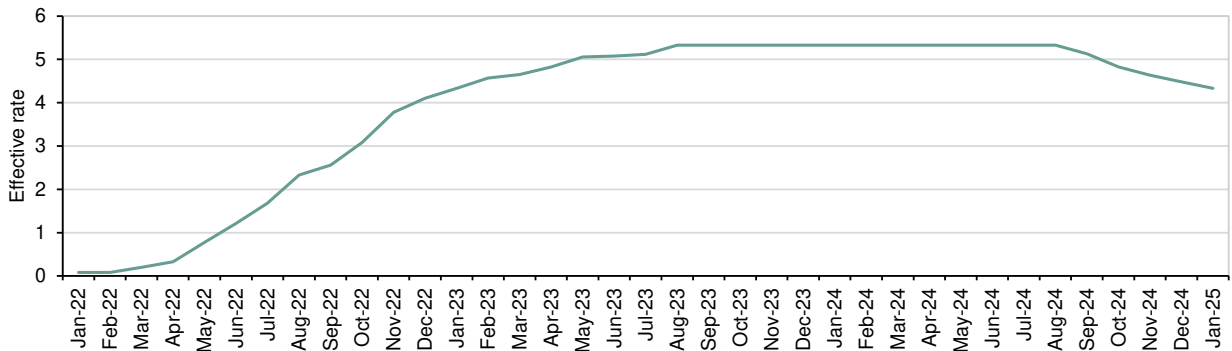
Key drivers for future performance

Primary Energy boosts the environmental and economic efficiency of high-profile US steel producers, such as Cleveland-Cliffs and US Steel. While the policy environment around the steel industry has become uncertain since the change in US president, the policy changes are aimed at protecting US steel-makers, as well as boosting demand for domestic production.

President Trump signed proclamations in February 2025 to impose a 25% tariff on all steel imports into the US, without exemptions for any countries. This is a reversal on previous exceptions, which included Canada, Mexico, the EU, the UK and Japan. While the final shape of the policy (and any exclusions or reversals) is uncertain, it is possible that these changes could result in increased demand for US-produced steel as consumers turn to domestic suppliers to avoid import duties. The expansion of domestic production to displace imports is one of the likely aims of the policy, and higher steel production volumes would present Primary Energy with options for further growth.

The net potential rise in demand for domestically produced steel is uncertain and depends on a number of factors. General economic growth is important, and the monetary policy environment is becoming more favourable (the US Federal Reserve has been easing interest rates since September), plus the backlog in infrastructure spending could also boost steel demand. Rising domestic steel prices could have a negative effect if they make domestic steel consumers less competitive, particularly in export markets, although the displacement of imports will potentially more than offset this.

Exhibit 1: Monthly effective Federal funds rate



Source: Statista, Edison Investment Research

Oliva

Introduction to Oliva – asset video



Source: SEEIT

Oliva had an equity value of c €132m at H125 (with no project level debt), down from c €151m at FY24 due to a one-off valuation impact (discussed below) and broadly in line with c €129m at FY23. Oliva consists of multiple sites which operate an integrated energy generation and waste treatment facility servicing Spain's olive industry, comprising a co-generation facility (where waste heat is also utilised to dry olive pomace, enabling the secondary extraction of olive oil) and a biomass plant, with combined annual energy production of 750GW. The asset structure demonstrates strong operational synergies between renewable energy generation and industrial processes.

Regulatory framework and revenue stabilisation

A significant development during 2024 for Oliva was the restructuring of Spain's Ro (return on operations) regulatory payment scheme. Initially characterised by high-revenue volatility, the regulatory update has introduced a more transparent, formula-driven remuneration system. While this enhancement brings greater predictability to cash flows, the revision notably excluded anticipated compensation for gas distribution costs, resulting in a one-time valuation impact of £23m.

Revenue structure analysis (at 30 June 2024, regarding CY23)

The revenue model comprises three primary streams, providing diversification and regulatory protection:

- RoRi payments constitute the largest component at approximately 49% of revenue. These regulatory payments for combined heat and power (CHP) and biomass assets incorporate adjustments for electricity sales and operating costs, including natural gas and EU allowance emission certificates. This mechanism delivers long-term EBITDA stability throughout the remaining asset life.
- Electricity sales generate approximately 35% of revenue, predominantly through grid sales from both biomass and CHP operations. While exposed to market pricing, this exposure is effectively mitigated through the RoRi mechanism and strategic hedging policies.
- Oil sales contribute approximately 12% of revenue through orujo oil production, marketed via short-term contracts. The pricing structure has the potential to provide some natural offsets against fuel supply costs through its correlation with biomass costs.

Operational performance and risk management

Recent performance has exceeded SEEIT's budget expectations, primarily driven by successful hedging strategies that

have enhanced operational margins. Management expects it to continue to deliver further margin improvements as well as de-risking olive feedstock procurement. The team uses a strategy of strategic stoppages, which allows for a reduction in exposure to short-term price drops where the CHP plants would be running at a loss. These procurement optimisation measures are expected to continue to deliver improved margins and risk reduction benefits.

Key drivers for future performance

Oliva has the ability and flexibility to enhance its profitability through strategic stoppages, avoiding the sale of electricity back to the grid at peak times during the day. Spain has large amounts of solar that will be producing at peaks levels in the middle of the day, in turn bringing down power prices. The ability to operate when power prices are at the highest possible levels therefore enables the site to maximise its operating profits.

Onyx renewable

Introduction to Onyx – asset video



Source: SEEIT

Onyx represents a strategic growth platform, of on-site solar and storage, within SEEIT's portfolio with an equity value at H125 of c \$378m (21% of total portfolio), up from c \$255m at FY24, and c \$51m project-level debt (excluding its revolving credit facility). Onyx had delivered strongly on its 2024 targets at H124 and has made good progress on securing PPAs for 2025, and management therefore made an additional adjusted valuation upgrade of c £22m (on the back of an independent valuation being obtained). The company operates through a dual structure of operational assets and development projects (currently across 27 states). The investment employs an innovative funding approach, utilising short-term debt, SEEIT equity, as well as investment tax credits (ITCs), to finance construction, with subsequent refinancing through long-term project-level debt upon operational maturity.

Operational performance and growth

During H124, while operational assets underperformed budget expectations due to reduced solar resource and site-specific technical issues, the platform demonstrated strong growth in development momentum, adding 14MW of operational capacity. This expansion underscores the platform's effective execution of its development strategy.

Revenue structure analysis (at 30 June 2024, regarding CY23)

Project portfolio (84% of investment value)

The operational and development project portfolio demonstrates strong revenue visibility through two primary streams:

- PPAs constitute approximately 93% of asset revenue, characterised by fixed indexation and typically spanning 20 years, with the current portfolio maintaining a weighted average duration of approximately 18 years. These agreements provide stable, long-term contracted revenue streams.
- Solar renewable energy credits generate approximately 7% of asset revenue through state-specific regulatory frameworks, providing additional revenue through marketable credits per megawatt-hour of renewable generation, however these only apply to certain sites in states that recognise RECs .

Development platform (16% of investment value)

The development arm maintains three distinct revenue streams:

- Asset management fees represent the largest component at 52%, generated through operational portfolio management services.
- Engineering, procurement and construction (EPC) development margins contribute 33%, realised upon the commercial operation date of delivered assets.
- Asset sales account for 15%, derived from pipeline development disposals, with enhanced returns following the June 2023 Blackstone development platform acquisition.

Investment strategy and risk management

The platform's valuation incorporates assumptions for construction and development projects achieving operational status within defined time frames. This structured approach to development, combined with the high proportion of contracted revenue in operational assets, creates a balanced risk-return profile.

Capital structure

The financing strategy demonstrates sophisticated capital management, utilising flexible funding during construction phases before transitioning to optimised long-term project financing. This approach enables efficient capital deployment while maintaining appropriate risk parameters for operational assets.

Key drivers for future performance

Onyx acts as a service model and is benefiting from macro themes of electrification, energy security (through on-site generation), grid decarbonisation requirements as well as grid localisation. The US is seeing a heightened demand for on-site generation, of which solar is the leading technology, due to the recent increase in data centres. On-site solar generation offers both reduced costs and greater local grid stability.

RED Rochester

Introduction to Red Rochester – asset video



Source: SEEIT

RED Rochester held an equity value of c \$281m at H125 (18% of total portfolio), up from c \$252m at FY24, with c \$92m of project-level debt. RED is a leading North American district energy system operator. The site underperformed against management's expectations in H125, with projected EBITDA approximately 13% below budget expectations. This decline reflects weaker than expected demand from a key customer and elevated maintenance costs, although management views these challenges as temporary.

Revenue structure analysis (at 30 June 2024, regarding CY23)

The business model demonstrates strong contractual foundations with built-in inflation protection, servicing over 120 commercial and industrial customers. The revenue structure comprises three primary streams:

- Capacity-based charges constitute the largest revenue component at approximately 62%, derived from predetermined tariffs based on service delivery costs and customer demand profiles.
- Fixed charges generate approximately 30% of revenue through demand-independent fees, providing baseline revenue stability.
- Overhead charges contribute approximately 8% of revenue through fixed mark-ups on utility bills, offering additional revenue consistency.

Contract security and growth potential

The revenue model is underpinned by 20-year contracts without break clauses, providing exceptional long-term visibility. The March 2024 portfolio valuation incorporates contract extension assumptions, while future cash flow projections include growth opportunities through capital enhancement projects, such as the forthcoming CHP plant. However it is worth noting that these future cash flow projections are both probability weighted and conservative.

Performance enhancement initiatives

Management has implemented a dual-track strategy to address the current underperformance. Negotiation of tariff amendments across the customer base is expected to share maintenance costs with customers and better align revenue with inflation of costs and comprehensive cost rationalisation and performance optimisation measures are being executed to support near-term results.

Key drivers for future performance

Li-Cycle, one of RED's largest customers, had been significantly expanding its facilities through the construction of a new hub processing centre. Construction has seen delays over the last year, but, once the hub is completed, RED will benefit from a substantial increase in demand, boosting the site's performance. Li-Cycle recycles lithium batteries and should benefit from macro trends of electrification despite the electric vehicle market being slightly out of favour recently.

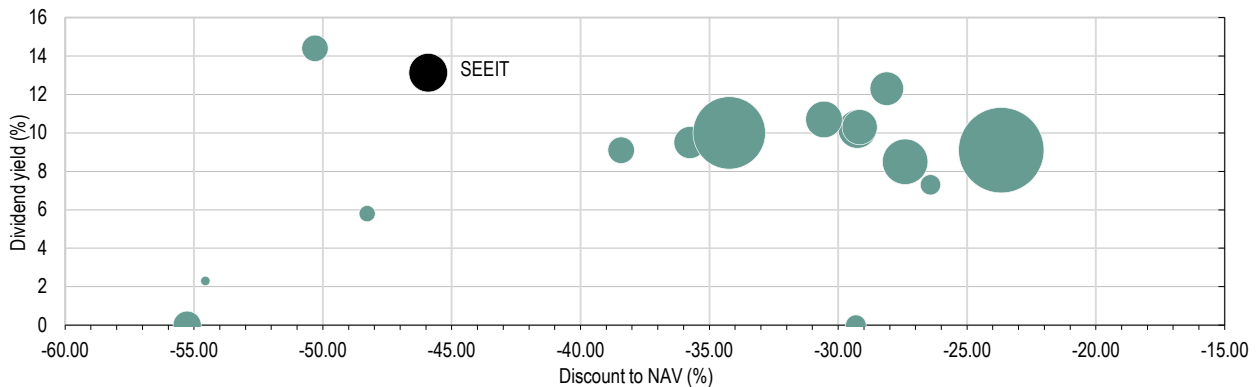
Driva (previously Värtan Gas)

Driva held an equity value of c SEK969m at H125 (6% of the total portfolio), in line with FY24's c SEK940m and up from c SEK831m at FY23, and c SEK682m of project-level debt. Driva owns and operates Stockholm's regulated gas grid, distributing and supplying biogas to over 50k residential, commercial, industrial, transportation and real estate customers. Stockholm is seeing an increasing rise in industrial firms moving outside the city, where the gas grid does not reach. To take advantage of this trend, Driva is delivering gas directly to its customers as a service. This is enabling the company to grasp a wider customer base. The company is also moving into the energy-as-a-service space, benefiting from the macro trend of decarbonisation and enabling cost reduction.

An outlier compared to the wider sector

The chart below plots the major constituents of the AIC Renewable Energy Infrastructure sector, with the vertical axis representing dividend yield (%) and the horizontal axis representing discount to NAV (%). The size of the investment trust in terms of market capitalisation is represented by the bubble size, with SEEIT shown in black. The funds further to the left of the chart trade at the largest discounts to NAV, with two relatively small funds in this territory (explained in part by the scale pressure on smaller trusts) and two other funds trading at a large discount. These are battery energy storage funds (GRID and Gore Street Energy) that have faced headwinds in terms of competitive pressures to their business models from lower gas prices and other factors. SEEIT, in comparison, is diversified by both technology and geography. It also has a relatively mature earnings model, being largely unaffected by merchant power prices, as it supplies energy efficiency as a service directly to its connected counterparties.

Exhibit 2: Discount to NAV against dividend yield of AIC Renewable Energy Infrastructure sector peer group



Source: Morningstar, Edison Investment Research. Note: The size of the investment trust in terms of market capitalisation is represented by the bubble size.
As at March 2025

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