



Warren Buffett Is Betting on Solar: Should You?

Description

In his annual shareholder meeting last week, Warren Buffett reiterated his interest in the renewable energy sector, saying that company was prepared to deploy tremendous amounts of money to expand the energy grid and deploy more renewable solutions moving forward.

By most measures, Buffett's conglomerate is one of the largest energy companies in North America. The company owns and manages more than 10 energy companies, with some of the largest utilities in the Western and the Midwestern U.S. This enthusiastic expansion and investment in renewables isn't driven solely by a desire to save the world. Rather, it's an indication that Buffett is doing what he does best: making money.

Here are three reasons why Buffett may be betting on solar and why green energy could be attractive investments for the average investor as well:

Production costs are plummeting

According to Buffett's 2016 shareholder letter, the energy game is changing. Distributed production of electricity through rooftop solar panels and independent wind turbines means that customers finally have an option that extends beyond their local utility.

Meanwhile, Deloitte predicts that government subsidies will make the renewable energy sector competitive with the traditional grid within a few years — a phenomenon known as “grid parity.” There's no doubt that customers will gravitate toward the cheapest source of energy, which could soon be solar.

Bloomberg reports that the average inflation-adjusted cost of utility-scale solar panels dropped from \$1.90 per watt to \$0.30 over the past eight years — a jaw-dropping 85% decline in less than a decade. This makes it cheaper to buy solar panels in bulk and operate industrial scale solar farms for power generation just as the demand for energy rises.

Demand explosion

During the shareholder meeting, Buffett said the demand for energy has flatlined in recent years, but will likely to pick up again over the foreseeable future. The demand for more electric vehicles and data centers will eventually push the need for energy far beyond current levels. According to McKinsey, electric vehicle charging stations alone will contribute 6.4% of total energy consumption across the world by 2050.

The sector is currently undervalued

The solar energy sector hit a rough patch last year. **TransAlta Renewables Inc** ([TSX:RNW](#)) and **Northland Power Inc.** ([TSX:NPI](#)) were down 25% and 8.5%, respectively. **Canadian Solar**, a pure-play solar company listed on the Nasdaq, was down 16% over the same period.

Calgary-based TransAlta currently trades at a price-to-earnings ratio of just 15. Over the past six years, the company's dividend has compounded at an annual rate of 6%, and the dividend yield is currently close to 6.8%. It's an incredibly robust and promising stock that seems to be underappreciated at the moment.

Similarly, Northland trades at a PE ratio of just 12 and offers a dividend yield of over 5%. The company has an attractively thick operating margin (45%) and a handsome rate of return on equity (27%), but is saddled with five dollars of debt for every dollar in equity.

If I had to pick, I'd pick TranAlta based on its track record, dividend, stable outlook, and economies of scale. However, both companies are excellent proxies for the ongoing renewable energy boom sweeping the globe. As demand for alternative sources of energy rises, either through regulations or organic need, both companies will benefit from their robust supply networks built over decades.

2018 was a good time to pick up both stocks. Energy investors could snap up renewable assets at bargain prices.

Buffett was on an energy spending spree throughout the year. His utility company, Nevada Power, signed a deal to build more than one gigawatt (GW) of new large-scale solar in the United States last year. Meanwhile, Buffett's MidAmerican Energy Company announced that it will become the first U.S. utility to source 100 percent of its customers' electricity needs from renewable sources when its \$922 million wind farm is completed in 2020.

The fact that the world's most famous value investor is pouring billions into this industry is a clear indication that assets are attractively priced.

Bottom line

Buffett's enthusiasm for the renewable energy sector over the past year indicates that one of the smartest investors in the world sees value and tremendous opportunity here. Regular investors shouldn't overlook the same opportunity.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. TSX:NPI (Northland Power Inc.)
2. TSX:RNW (TransAlta Renewables)

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1. Msn
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