3 Reasons Why Lower Interest Rates Make Renewable Energy Stocks Look Like Great Investments

Description

Earlier this week, the Federal Reserve Open Market Committee (FOMC) met to review its outlook for the economy and discuss what actions it should take to help it achieve its long-run goals of price stability and sustainable economic growth.

The takeaway from this week's meeting, one of eight to be held this year, was that there is now a greater chance than before that central banks will be lowering rates this year.

Some experts suggest that "The Fed" may be cutting rates by as much as 50 basis points, or one-half a percent, by the time the year is through.

Markets thus far have rallied on the news, because interest rates make the cost of borrowing money less expensive, which basically helps everyone in the economy from businesses to individual households and governments, too.

But why does the Fed feel the need to be taking on an "accommodative policy" to cut interest rates to begin with?

The Fed cuts its official policy rate when the economy isn't doing so well, so it tries to "ease" the financial burden of taking on debt, in other words, adopting an "accommodative monetary policy."

But the latest Fed announcement tilts the scales fairly firmly in favour of renewable energy stocks.

Utilities provide good proxies for bond investments

When interest rates decline, utility stocks typically tend to do well.

There are several reasons for this, but one of them is that lower interest rates make the prospective returns on fixed-income securities look less attractive, and conversely, utility stocks that tend to pay higher dividends on average tend to look much better by comparison.

Take, for example, **Brookfield Renewable Partners** (TSX:BEP.UN)(NYSE:BEP), which currently yields 6.12% annually.

Why would an investor buy a Government of Canada 10-year bond yielding just 1.42% when they could participate as owners in a promising renewable energy company paying out a 6.12% dividend?

Renewable energy projects are very capital intensive

Unlike certain other businesses — like those operating in the retail or services sector — developing and seeing to completion a large renewable energy project can be an extremely capital-intensive process, often taking years before investors begin to see returns.

What this means is that renewable energy companies often have to take on large sums of debt to finance these types of projects, but with interest rates appeared headed back towards historically low territory, the cost required to finance these types of large projects starts to become a lot cheaper on a relative basis.

Renewable energy is market agnostic

Because of where renewable energy currently lies in terms of its industry lifecycle, it's still relatively market agnostic, meaning that the success or failures of a company like Brookfield is going to have less to do with whether GDP is growing or shrinking and more to do with whether the project has been properly researched, developed, and executed.

In an environment where unemployment is rising and the economy is faltering, these types of factors are going to have less of an impact on renewable energy companies and companies like BEP than they are for certain other economically sensitive sectors of the market.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

TICKERS GLOBAL

1. NYSE:BEP (Brookfield Renewable Partners L.P.)
2. TSX:BEP.UN (Brookfield Renewable Partners L.P.)

PARTNER-FEEDS

1. Msn
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