Do you need a chief capital officer?
How to meet the financing challenges of capital-intensive cleantech companies

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An emerging solution for fast-growing cleantech companies in capital-intensive segments

Cleantech companies are developing the technology solutions that will enable the global transition to a resource-efficient and low-carbon economy. Cleantech encompasses such industry segments as renewable energy, energy efficiency, energy storage, energy management and water. While companies in all cleantech segments need new investment capital, certain ones have considerably greater capital requirements. Among them are companies that must achieve scale in manufacturing or delivery or that must participate in infrastructure-sized projects, such as those in the energy generation and manufacturing segments. It is with this latter group of companies in mind – those with the highest capital requirements – that the following ideas are presented.

Just as the world thirsts for clean energy, the companies striving to provide it thirst for capital. The structure of the venture capital and private finance industry was largely established in the 1980s to serve information technology companies based mainly in the United States. Since that time, business has become more globalized, and companies now need to address global markets and global competition much earlier in their life cycles. Further, because of evolving regulations and more exacting investors, finance departments face ever-increasing demands.

The result is that today, all emerging companies require more capital before they go public. In a typically more capital-intensive industry such as cleantech, the challenges are even greater. The CFO and treasurer of a cleantech company may know a good deal about capital formation. But with the need for a more robust finance function and an expanded role for the CFO, they are already juggling significant calls on their time. Thus, cleantech companies are left facing some inescapable questions: are our capital formation requirements so omnipresent, so significant and at the same time, so essential to strategy that they beg for focused attention and specialized skills? And do we in fact need a chief capital officer (CCO) with those specialized skills to focus exclusively on capital formation and deployment?

An industry in need

In the traditional energy generation sector, building the coal, natural gas and nuclear plants that supply us with power today has required billions, if not hundreds of billions, of dollars in equity and debt financing, whether public, private, project-related or tax equity. The same scale of investment is required now for large-scale infrastructure changes in the global grid, in fossil and bio-based fuels, and in automobiles, whether gas-powered or battery-powered.

The most capital-intensive segments of cleantech include renewable energy production, biofuel commercialization, electric-vehicle charging and other grid development or enhancement. Over the coming years, each will likely require many hundreds of billions of euros, yen, US dollars and renminbi spanning investment horizons of a decade or more.

Within certain segments of cleantech, the capital needs are enormous because most of the technologies and infrastructure that will power the future are still in early-stage development or just entering commercialization. Consider the companies whose technologies call for extensive manufacturing, large-scale power plants or bio-refineries or wide-ranging infrastructure for distribution. For such companies, capital requirements become even greater as they move into the commercialization phase. Still others will need a strong capital base in order to provide, for example, warranty assurance in wind and solar. Obviously, demand for capital on this scale goes far beyond customary venture capital, IPO or other traditional sources of financing for high-growth companies.

Financing of this magnitude typically calls for a project-financing approach. The challenge here, however, is that classic project financing typically accrues only to ventures with proven technologies and secure cash flows. Even a demonstration-scale project can involve hundreds of millions of dollars, and it still may fail. Clearly, the rewards of getting it right are also much greater, particularly for global solutions, but the evolving nature of the capital markets and a still-nascent understanding of the capital formation, regulatory changes, governmental support and technological risks involved make navigating these financial waters a much more complicated proposition. For the industry, this leaves a funding gap that will require focus, innovation and no small degree of determination to fill.

One obvious piece of the solution is government financing. Since it is in the public interest to put in place the engineering and infrastructure needed to fulfill the promise of cleantech, it is entirely appropriate that governments around the world provide support for such projects. But government grants, tax incentives, subsidies and regulatory inducements are only a partial solution and one that has come under severe pressure in the wake of the global economic downturn that began in 2008.

For the capital-intensive sectors of cleantech to gain real traction, their development must be backed by the full faith and credit not only of governments but also of the private sector. Over the long term, financing the future of renewable energy will involve a complex interplay among diverse capital sources. These will
ultimately include banks, international investors, corporations, legacy utilities and energy firms, and broad industry coalitions, as well as local, regional and national governments. Securing capital from one source will in large part become dependent on securing financing from the others as well. At the company level, orchestrating such a symphony will require a conductor of considerable talent.

But do we need a CCO?

The financing needs of a company pursuing the commercialization of cleantech infrastructure are immense, and the ecosystem necessary to satisfy them will be complex. Hence the question: do cleantech companies need a C-level executive whose sole purpose is to tend to the strategy and practice of capital formation and deployment?

The immediate response may be to say no, capital formation is the job of the CFO or CEO. That may well be so in much larger, well-developed industries and businesses. But look again at the unique situation of cleantech companies, especially those in the renewable energy segments, which tend to be young and fast-growing.

While the CFOs of such companies may play an important role in financing, their primary charge in most cases is to create the well-honed reporting, compliance and control-oriented finance function required to facilitate fast growth. This is a vital role, without which few firms would be able to attract the necessary baseline investment. At the same time, however, particularly in a high-growth company, it is also a highly specialized and demanding role that can leave little time for much else. For example, the CFOs of high-growth companies are increasingly required to undertake the financial integration of the company's global operations and activities. Such duties reflect a largely inward focus, whereas the responsibilities of the chief capital officer are primarily focused outward. Among them are marketing the company to potential investors and partners and negotiating the eventual deals that will provide the needed capital.

The other alternative is to assume that capital formation is one of the primary responsibilities of the CEO. It is true that for many companies, particularly in their early stages, the CEO tends to act as the CCO, treating the function almost as a full-time and continuous duty. However, as companies mature, he or she quickly becomes saddled with too broad a range of duties to be able to focus sufficient attention on the formation of capital. So at some point, the CEO must choose whether to retain capital-raising as a primary role or to bring in a CCO.

Arguably, however, the role is best filled by someone who is a terrific company spokesperson and salesperson, who has very broad financial industry contacts, who can do both business development and project development and can negotiate complex financing structures; someone who is able to travel constantly (recognizing that the sources of capital are now worldwide and highly dispersed), has international savvy and can combine a broad range of financial instruments into a coherent whole that can be readily explained to investment bankers. If that sounds like your current CEO or CFO and that person can do all those things in addition to his or her regular day job, you are in great shape. Otherwise, you might well consider whether you need a chief capital officer.

Defining the role

Analyzing the responsibilities of the CCO function, a number of essential attributes become clear. A CCO, must, for example:

- **Know the markets.** First and foremost, the CCO must have in-depth knowledge of global capital markets, which is more than simply a theoretical understanding of funding mechanisms. Rather, any executive performing the role must be at home in the marketplace. He or she will have considerable experience and even credibility and clout with investors and analysts. And most important, the CCO must be able to sell to the disparate community of investors and lenders.

- **Understand counterparty needs.** A CCO will recognize that satisfying a company’s appetite for capital will mean attracting a wide range of investors. A CCO may be talking to a syndicate of investment banks in the morning and a pension fund manager in the afternoon, or a potential merger partner one day and a government agency the next. The CCO must know how to speak to each class of investor or partner in the most appropriate and appealing terms.

- **Be capable of innovation.** Many of the templates and models for the types of financing transactions the cleantech industry needs either have not yet been created or are not yet well understood. Further, the CCO must understand how to manage the process of raising additional capital with the longer lead times required for new sources compared with the venture capital that probably funded the company until this point.

- **Understand corporate and project development.** As cleantech evolves, its capital needs and its future will be shaped by acquisitions, partnerships and alliances. The CCO must be experienced in navigating the ins and outs not only of M&A, but also of project finance, leverage, tax issues and cross-corporate boundary collaboration within extended commercial ecosystems.

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Setting the capital agenda
Cleantech is not the only industry facing capital challenges. In fact, all companies must remain ever at the ready for any actions necessary to secure and optimize their capital base. Failure to pay adequate attention to key capital issues leads to inefficiencies, costs and risks that hamper performance and degrade shareholder value.

- Stress and distress — e.g., liquidity issues and turnaround plans
- Customer and supplier analysis
- Preserving tax assets and minimizing costs
- Refinancing or restructuring debt, equity and other obligations
- Dealing with stakeholder relationships and pressure
- Dispute resolution

- Optimizing asset portfolio
- Delivery of synergies and effective integration
- Improving working capital and releasing cash
- Optimizing capital structure
- Optimizing tax and corporate structure

Practically speaking, companies — cleantech and otherwise — should be thinking about their capital base in four dimensions:

- Raising capital — Are you speaking the language of investors? Have you adjusted to a new world order in which many financing sources may not be domestic? Are you presenting potential investors with attractive opportunities? Do you fully understand the range of available financing options, and are you tapping the most efficient sources?

- Investing capital — Are your investments the most appropriate for your organization's capabilities? Are you conducting proper due diligence and risk mitigation? In general, are you evaluating your portfolio of investments through the lenses of global markets and investors? Are your investments the most appropriate for your organization's capabilities and are you paying the right price?

- Preserving capital — The preservation of capital requires that companies continuously reassess their strategies, markets and balance sheets for strengths and weaknesses. Are you conducting such analyses? Do they extend beyond the business itself to consider external forces such as the capital position of competitors, the supply chain and even customers?

- Optimizing capital — Do you conduct regular assessments of capital efficiency? Are you ensuring that capital is being deployed at optimum efficiency within your risk tolerance? Are you using the correct mix of instruments and risk/return profiles? Are you pursuing tax efficiency?

A strong capital agenda needs to be at the heart of all strategic boardroom and management decisions. It helps companies consider their issues and challenges and more importantly, understand their options to make more informed strategic capital decisions.

Over time, as the company, its competitive conditions and its strategies evolve, emphasis will likely shift from dimension to dimension. But in general, regardless of their industry, companies must be cognizant at all times of these key aspects of an effective capital agenda. Accordingly, the CCO position may well have appeal beyond cleantech.
Know financial modeling. The CCO must be an expert at working with other members of the management team to understand market dynamics and design financial models, at both a company level and a project level. Such models will be essential in presentations to a range of potential investors.

Work well with bureaucracies. Governments the world over will contribute substantially to capital formation in cleantech. However, their participation will vary by nation and by sector or technology. In some instances, governments will offer outright grants, low-cost loans, loan guarantees, tax breaks or other financial inducements. They will also, most certainly, take steps like implementing regulatory frameworks that support cleantech. Therefore, the CCO must be a diplomat, skilled in collaborating with government. Moreover, he or she must be detail-oriented and able to comply with what will likely be an array of complex requirements if financial support is received from the government.

Know the art of the deal. The CCO will need to build relationships with potential investors around the world. Further, he or she must be able to communicate investment opportunities to investors, as well as lead in the creation and negotiation of the financial instruments and deal structures necessary to obtain capital. Capital formation responsibilities will include plain vanilla equity issuance and bank loans, but also more complex and unusual transactions. Ultimately, the CCO must be a leader, capable of inspiring confidence both within and outside the organization.

Live and breathe capital-efficiency and finance-effectiveness. The CCO’s job is to plan proactively for the company’s ongoing capital needs – not just for today, but for the longer term. He or she will work full-time not only to secure capital but also to ensure that such a scarce commodity is always efficiently deployed (see “The range of capital challenges,” p. 4).

What begins to crystallize is the idea that the CCO function is an extraordinary endeavor. The exact mix of qualifications for the role will vary from company to company and by technology focus. But by force of necessity, we can expect to see a cadre of executives with these skills develop in cleantech over the next several years.

Getting the job done

It is one thing to understand the role of the CCO. But it is quite another to find someone who meets the chosen criteria and then to integrate the position into the ongoing workings of a typical high-growth, capital-intensive cleantech company.

Indeed, such an executive will probably be a relatively rare commodity. And bringing in a CCO with all of the requisite attributes from outside the company will likely prove a costly proposition. For this reason, it will be crucial to scope out a clear mission for the role, as well as a transparent means of measuring its value.

As important as finding the right person will be developing a way to incorporate the role into the managerial framework. Should such a position be imposed by fiat, it is likely to stir up a spate of bad feeling. In particular, for the existing CFO and treasurer, the move could signal demotion rather than the addition of a necessary and complementary position. Consequently, it is vital for these executives to participate in the discussions to identify the need for a CCO and develop the job description. Once the scale and scope of the capital formation and deployment challenges are articulated, these executives are likely to come to the same conclusion – it is an essential role. The only remaining question will be what route will best satisfy this organizational need.

Boardroom issues

- Is a lack of capital hampering our ability to grow?
- Do we have cause to review our capital structure at the board and operational levels?
- Do we have sufficient skills in global capital formation?
- Are there any executives in-house with the requisite skills?
- Given existing demands, does the CFO have the bandwidth to add this charter?

A discussion worth having

Certain segments of the cleantech industry are capital-starved and will remain so for the foreseeable future. And in each segment, the companies are unique in terms of the in-house capabilities they already possess. But in all cases, consideration of the role of the CCO should prove a powerful strategic exercise, if nothing else.

For some companies, the CCO concept may prove intriguing but impractical. For others, the idea may be useful only inasmuch as it serves to evolve the existing corporate seating chart. But still others are likely to find the concept so appealing that they begin taking steps to implement the role, whether as part of the C-suite or as part of the finance function, perhaps reporting to the CFO.

Whatever the case, the concept deserves careful consideration by cleantech companies that plan for significant capital formation. In fact, we believe that given the capital needs of the cleantech industries, the starting point should be less “Do we need this position?” and more “Why don’t we have this position already?”
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EYG No. FW0002

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