



Glasgow City Council

Strathclyde Pension Fund Committee

Report by Director of Strathclyde Pension Fund

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**Item 5**

11th September 2024

**Direct Impact Portfolio (DIP)  
Investment Proposal – Quinbrook Renewables Impact Fund II**

**Purpose of Report:**

To set out a proposal for an investment of £60m within DIP.

**Recommendations:**

The Committee is asked to **APPROVE** an investment of £60m in Quinbrook Renewables Impact Fund II by DIP.

Ward No(s):

Citywide: ✓

Local member(s) advised: Yes  No  consulted: Yes  No

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# 1 Background

## 1.1 Portfolio Establishment

In December 2009, the Strathclyde Pension Fund Committee agreed to establish a New Opportunities Portfolio (NOP) with a broad remit to invest in assets for which there was an attractive investment case but to which the current structure did not provide access.

## 1.2 Review

The NOP strategy has been subject to 3-yearly reviews with the name changing to the Direct Investment Portfolio in 2015. The most recent review was concluded in November 2021. This made no change to the objectives, structure, overall size parameters, risk and return parameters, or governance structure, but did result in an increase in the individual investment size parameters and a further name change to the Direct Impact Portfolio (DIP).

## 1.3 Implementation Framework

DIP investment proposals are assessed on their own merits within an agreed implementation framework based on SPF's overall risk-return objectives and specific DIP parameters.

The framework agreed at the 2021 review is summarised below.

Direct Impact Portfolio	
<b>Objectives</b>	Primary objective identical to overall SPF investment objective. Secondary objective of adding value through investments with a positive local, economic or ESG (environmental, social, governance) impact.
<b>Strategy &amp; Structure</b>	In line with SPF risk-return framework but focused on the UK and the Equity, Long Term Enhanced Yield and Short Term Enhanced Yield asset categories.
<b>Risk and Return</b>	Portfolio benchmark return of <b>CPI +3% p.a.</b> Individual risk and return objectives for each investment.
<b>Capacity</b>	Target allocation of <b>5%</b> of total Fund (based on Net Asset Values). Range of <b>2.5%</b> to <b>7.5%</b> of total Fund.
<b>Investment Size</b>	Target: <b>£30m</b> to <b>£100m</b> Minimum: <b>£20m</b> Maximum: greater of <b>£250m</b> or <b>1%</b> of Total Fund Value
<b>Decision Making</b>	3 stage process with review and satisfactory due diligence by officers, followed by a presentation to the Sounding Board before a proposal is taken to Committee for approval subject to completion of legal documentation.
<b>Monitoring</b>	Includes individual investment reports, participation in advisory boards, and a quarterly DIP monitoring report which is reviewed by the Fund's Investment Advisory Panel.
<b>Co-investment</b>	Existing co-investment programme should be extended in order to maximise its effectiveness, subject to development of a detailed proposal.

The following proposal has been assessed using this framework and has been reviewed by the SPF Committee Sounding Board.

## 2 New Investment Proposal

### 2.1 Key Terms

<b>Name</b>	<b>Quinbrook Renewables Impact Fund II</b>
<b>Investment vehicle</b>	Jersey Limited Partnership
<b>Manager</b>	Quinbrook Infrastructure Partners
<b>Sector</b>	Renewable Energy
<b>Investment objective</b>	To construct a portfolio of renewable energy generating assets, battery storage and grid support infrastructure
<b>Term</b>	10 years (plus up to 3x1 year extensions)
<b>Target size</b>	£500m (Hard Cap £1bn)
<b>Proposed DIP investment</b>	£60m
<b>Target return</b>	Internal Rate of Return (IRR) of 9.9% (Net) / Cash Yield 6%+ p.a.

### 2.2 Investment Summary

Quinbrook Infrastructure Partners (QB) is a specialist value-add investment manager focused exclusively on the infrastructure required to deliver the energy transition, by originating, constructing and managing direct investments in low carbon and renewable energy (RE) infrastructure assets.

The QB Renewables Impact Fund II (QRIF2) is the successor fund to QRIF1 in which DIP committed £50m in 2020 (of a total of c.£600m from 12 investors, including 10 UK LGPS funds). QRIF1 has performed very satisfactorily to date.

Both QRIF funds are primarily UK-specific successors to 3 other prior QB funds, including its largest and flagship vehicle, the QB Low Carbon Power Fund (QLCPF). This fund successfully raised US\$1.7bn of investor commitments for deployment in the US, UK and Australia.

Like QRIF1, the investment strategy for QRIF2 is to create a portfolio of mainly UK RE generating assets, battery energy storage systems (BESS) and grid support infrastructure assets, which will support the UK in achieving its Net Zero emissions target by 2050. Up to a maximum of 15% of the fund however may be invested in the Republic of Ireland.

A commitment by the Direct Investment Portfolio of £60m to the QRIF2 fund is proposed.

More information on the Manager is included in **Schedule 1**.

### 2.3 Investment Rationale

For the QRIF2 fund, QB will be targeting investment opportunities in the decarbonisation of the production and management of energy. They will do this by investing in established renewables technology including solar, battery

storage and/or onshore wind infrastructure, either individually or in combination (e.g. co-located solar and battery storage) in addition to grid support assets and distributed energy solutions. The fund will also be seeking opportunities for the decarbonisation of transport and in emerging opportunities in major equipment and materials recycling, resource recovery and re-use in the circular economy. These target sectors are presenting attractive opportunities for asset managers with the appropriate expertise.

The requirement for grid support infrastructure is a consequence of the UK's shift from a mainly coal and gas-fueled power generation system to the current, more intermittent RE platform. The intermittency of the latter is in contrast to the steady state, base-load output of the traditional thermal-based (but environmentally harmful) power generation of the past, however it does create grid reliability/stability issues.

The National Grid (NG) has a regulatory requirement to ensure that distributed electricity is maintained within very narrow bands in respect of both frequency & voltage, failing which industrial and domestic consumers can suffer blackouts.

Synchronous condensers are a robust, long-established and relatively simple technology, which ensures the stability of the grid by generating inertia (the resistance to adverse changes) in the grid system. These assets are constantly on standby under long-term, inflation-linked availability contracts with NG, ready to intervene instantaneously and act to oppose any adverse movement in frequency &/or voltage away from the mandated levels.

QRIF1 successfully bid for 5 of these contracts from NG, including 4 in Scotland which are currently under construction, and is a market which QRIF2 intends to target again with several opportunities in its current pipeline.

Battery storage assets can also be used to assist to alleviate the high cost of electricity constraint payments. When weather conditions are favorable (i.e. wind speeds/solar irradiation are strong), the grid is unable to accept all the power generated by the RE sector. During the past decade, NG has required to compensate the renewables industry with c.£750m in constraint (or curtailment) payments, while the power potentially generated is also lost.

Commercial scale BESS projects can contribute to addressing this by either accepting excess RE produced when supply exceeds demand, or by discharging power in the opposite scenario. The assets can either operate in the open electricity market on their own account, or alternatively can bid for capacity contracts with NG to allow the latter to more effectively manage the grid. In this respect the inflation-linked revenues under such NG contracts effectively represent an availability contract and avoid merchant pricing risk.

QRIF2 will seek to develop and construct new assets through its partnerships with smaller developers and also via the opportunistic acquisition of underperforming, undervalued or distressed operating assets where the QB team believe they can apply their experience and expertise to identify solutions.

The manager has a well-developed pipeline of UK solar, battery, wind and grid support opportunities resulting from its QRIF1 activities and network of early-stage RE development partners. The team are confident they will be able to deploy the fund's commitments (even at the hard cap level).

## **2.4 Risks**

The main risks of the proposed investment in the QRIF2 fund are considered to be as follows:

- Origination Risk
- Development Risk
- Construction Risk
- Generation Risk

A summary of risks and key mitigants is contained in **Schedule 2**.

## **2.5 Projected Return**

The target (blended) return of the various elements of the fund's strategy is an IRR of 9.9% (Net). A Cash Yield of 6%+ p.a. is targeted with effect from the operational phase of the projects.

This return is slightly higher than DIP would typically anticipate for more generalist RE funds. This is due to the assets typically being late-stage development, pre-construction or (operationally) underperforming, combined with the higher returning, smart grid infrastructure assets. QRIF2's assets however will not benefit from the now discontinued RE subsidy regimes.

## **2.6 Exit**

QRIF2 has a fixed term of 10 years with an additional 3 one-year extensions. While QB will not actively seek disposals, the manager's experience has been that unsolicited offers are periodically received for certain assets. These will be actively considered if the terms are compelling and return enhancing.

## **2.7 Fees**

The Management Fee is fairly typical of DIP's experience for the RE sector and incorporates various discounts for existing QB and first close investors, as well as a scale discount in respect of the aggregated commitments of LGPS investors, which normally feature strongly with QB funds.

Carried Interest provisions also apply and have been structured at a relatively typical level for funds in the RE market.

Overall the fees are in line with DIP's experience in the RE sector and are considered satisfactory.

## **2.8 ESG and Impact**

QB was founded in 2015 to invest in the development of the lower carbon and renewables infrastructure required to deliver the energy transition. It seeks to contribute to the achievement of Net Zero emissions in its target markets whilst delivering attractive returns to investors and sustainable impact in terms of job

creation, local community benefits, biodiversity net gain and carbon emission reductions.

A summary of the fund's ESG and Impact factors is contained in **Schedule 3**.

## 2.9 Investment Size and Cash Requirements

SPF Fund value at 30th June 2024	£30,585m
DIP allocation (target 5% of main fund) NAV	£ 1,529m
Current DIP NAV	£ 1,528m
<b>NAV Range (Lower) 2.5%</b>	£ 764m
<b>NAV Range (Upper) 7.5%</b>	£ 2,294m

## 2.10 Investment Strategy

The proposed investment falls within the Infrastructure/Renewable Energy sector and therefore the Fund's Long Term Enhanced Yield allocation. RE is a key area of investment focus for DIP.

Allocations following this investment based on SPF values at 30<sup>th</sup> June 2024 and total DIP commitments to Infrastructure/RE would be as follows:-

Infrastructure/Renewable Energy, £ in DIP	£1,259m
Infrastructure/Renewable Energy, % in DIP	58%
Infrastructure/Renewable Energy (DIP), % of Total Fund	4.1%
LTEY, % Total Fund (target 21.0%)	17.6%

## 3 Policy and Resource Implications

### Resource Implications:

*Financial:* Investment of £60m to be drawn as required. The fund's fee structure is considered to be in line with the market.

*Legal:* The investment will be subject to satisfactory completion of due diligence, including review and execution of appropriate legal documentation.

*Personnel:* None

*Procurement:* None

**Council Strategic Plan:** SPF supports the mission: ***to enable staff to deliver essential services in a sustainable, innovative and efficient way for our communities***. The LGPS is one of the key benefits which enables the Council to recruit and retain staff.

**Equality and Socio-Economic Impacts:**

*Does the proposal support the Council's Equality Outcomes 2021-25? Please specify.*

Equalities issues are addressed in the Fund's responsible investment policy.

*What are the potential equality impacts as a result of this report?*

No specific impact from this proposal.

*Please highlight if the policy/proposal will help address socio-economic disadvantage.*

The Manager has a policy to utilise local contractors and therefore to support local jobs wherever possible in the construction of assets.

**Climate Impacts:**

*Does the proposal support any Climate Plan actions? Please specify:*

The fund will be deployed in the RE and/or grid infrastructure sectors and therefore will have a direct impact on the UK's de-carbonisation objectives. This is consistent with Strathclyde Pension Fund's Climate Change strategy, which is being developed in line with Item 34 of the Council's Climate Action Plan.

*What are the potential climate impacts as a result of this proposal?*

The fund's investments will result in the reduction of carbon emissions from the power generating sector as well as improvements to the stability of the UK grid network.

*Will the proposal contribute to Glasgow's net zero carbon target?*

Yes, as detailed above.

**Privacy and Data Protection Impacts:**

To be fully provided for in the legal documentation for the proposed investment.

Are there any potential data protection impacts as a result of this report  
Y/N

N

If Yes, please confirm that a Data Protection Impact

N/A

Assessment (DPIA) has  
been carried out

#### **4 Recommendations**

The Committee is asked to **APPROVE** an investment of £60m in Quinbrook Renewables Impact Fund II by DIP.

<b>Schedule 1</b>	<b>Investment Manager: Quinbrook Infrastructure Partners</b>
<b>Schedule 2</b>	<b>Investment Specific Risks</b>
<b>Schedule 3</b>	<b>ESG and Impact</b>



### **Investment Manager: Quinbrook Infrastructure Partners**

Quinbrook Infrastructure Partners (QB) are RE specialists who are highly experienced in the development, construction and management of performing and/or underperforming operational power generating and grid infrastructure assets.

The firm was founded in 2015 by Managing Partners Rory Quinlan (RQ) & David Scaysbrook (DS) (the Founders) who have worked together for 30 years in the RE investment sector (including 5 years with Capital Dynamics at Senior MD level) immediately prior to forming QB.

The Founders have established, deployed and managed 4 previous co-mingled (i.e. funds with multiple investors) RE / low carbon infrastructure funds at QB as well as several other funds whilst employed at Capital Dynamics. They have raised commitments from >40 institutions (including £562m of a total of c.£600m from 10 UK LGPS funds in QRIF1, the predecessor fund) for investment into RE infrastructure projects since 2010. QRIF2 will be their fifth co-mingled investment fund focused on low carbon, RE power assets and their second to be deployed exclusively in the UK.

Together with the 4 other members of QB's Investment committee, RQ & DS have collectively deployed US\$5.6bn of equity across 230+ energy assets, primarily in the US, UK & Australia with both QB and previous employers. This includes >130 UK based power and renewables projects since 2000 across onshore wind, landfill gas, coal mine methane, hydro and reserve peaking power (the delivery of power at peak times via the generation and storage at off-peak times).

Quinbrook Infrastructure Partners are authorised and regulated by the Financial Conduct Authority .

### Investment Specific Risks

#### Origination Risk

The Manager has built a sizeable pipeline of opportunities through partnerships with smaller or less experienced developers. The vast majority of these will have multiple projects at various stages of development over which QB would require exclusivity before partnering with those developers, with contractual arrangements structured for alignment purposes to reflect the achievement of key development milestones. In this way if a number of projects were to fail to proceed for whatever reason, the overall effect on the pipeline of opportunities (or cost) wouldn't be significant.

#### Development Risk

This is the risk that the land, planning, grid connections and/or permit/licensing approvals required for a project to proceed are not obtained, or are secured with conditions which make the project unviable.

QB seeks to mitigate development risk either by acquiring outright, or by entering into partnerships with smaller developers thereby securing exclusivity over multiple projects in different assets, at different stages of development, locations, licensing authorities and/or power off-takers (energy companies or commercial consumers who buy the power) and the failure of any single development project will not adversely affect the overall portfolio of projects.

The firm has a highly experienced inhouse development team (Private Energy Partners) which affords much greater control over the progress and cost of development projects. Development risk is further mitigated through extensive due diligence undertaken throughout the investment, development and construction process. This is the essence of the QB team's expertise and their strong track record to date has been founded on investments in development stage opportunities.

#### Construction Risk

This is the risk of cost over-runs in the capital budget of a fully developed project and/or the cost of delays in completion. QB is expected to invest only where such construction costs can be fixed or capped and where they have experience and confidence in the construction methods, the contingency allowances and in the contracting parties themselves. The cost overrun risk is normally also mitigated through the use of retentions, guarantees and other forms of support in order to pass the majority of the risk to the construction contractor. QB however has a very strong track record of managing large and/or complex construction projects on time/within budget.

#### Generation Risk

The estimation of expected energy production is a key aspect of the due diligence process for the QB team and is where they see what they consider to be overly optimistic assumptions by developers or other parties. QB's extensive operating experience allows them to mitigate this risk.

### ESG and Impact

QB's core business is dedicated to building sustainable energy infrastructure and real asset-based solutions having a long-term positive impact on the climate, environment, local economies, and communities.

The firm was established as a specialist energy transition infrastructure investor focused on the development, construction, and operation of new assets and the building of scaled businesses that seek to sustainably and responsibly support the transition to Net Zero. It was established as a 'mission driven' organisation, with a fundamental commitment to sustainability and Responsible Investment (RI) which continued the Founders' pioneering support of RI in institutional investing that started with their influence at the inaugural RI summit in London in 2010.

QB's overarching objective is to create assets and businesses that progress the energy transition. This core thesis is set within a broader commitment to driving positive social, environmental and climate impact, delivered through active stewardship of assets. QB believes that through active management it can better drive outcomes aligned with its sustainability and impact goals.

All QB investments aim to be managed consistently with the firm's key objective to positively drive and accelerate the energy transition and thereby support key sustainability and climate focused United Nations Sustainable Development Goals (UN SDGs). RI is intrinsically tied to both short and long-term risk mitigation and to the creation of investment value on behalf of its clients.

QB targets investment in climate mitigation solutions that provide greater availability, affordability, reliability, and security of low or carbon free energy supply and greater energy efficiency, carbon emission reductions or avoidance.

The firm's strategies cover a wide range of impact-led goals, including support of a just transition, local jobs creation, preservation and skills training, development of sites within areas targeted within the UK for 'levelling up', development of key skills, innovation, support of local UK industries and enhancements to local energy security and health through lower pollution.

QB integrates awareness and management of sustainability-related factors throughout the investment cycle, in due diligence, Investment Committee decisions, internal and portfolio company operations, ongoing ownership and exit of invested assets and businesses and in its engagement with the wider community.

QB became a signatory to the PRI (UN Principles of Responsible Investment) in 2016 and has been awarded the highest rating (5\* from 2022 / previously A+) for each mandatory reporting year since. It is a supporter of the Taskforce for Climate-Related Financial Disclosures (TCFD) and a member of the Institutional Investors Group on Climate Change (IIGCC). Founder David Scaysbrook was a member of the inaugural UNPRI Infrastructure Advisory Committee and is Chair of the Advisory Committee of the Climate Investment Centre at Imperial College, London.