INDUSTRY TIMELINESS: 52 (of 93)

The Power Industry consists of a variety of companies that are engaged in either the generation or distribution of electricity. In most cases, the power is derived from sources other than fossil fuels. In fact, most members of the group produce electricity using alternative methods. These include solar, wind, geothermal, hydro, biomass, and hydrogen.

Despite all the actions being taken to reduce global warming, this Industry has not benefited to the degree that many investors would think. Indeed, the past five years have been difficult ones for this Industry. Global competition and overcapacity, has led to severe pricing pressures, in the solar sector. During this time frame, quite a few companies have either incurred large losses or have not been very profitable. A major headwind continues to be that fossil fuels, especially natural gas and coal, are often the cheapest ways to produce electricity. Nevertheless, technological gains have helped narrow the cost difference.

The Inflation Reduction Act (IRA) will likely have a significant impact on this entire sector. About $440 billion has been set aside for the purpose of making it cheaper for users to reduce their dependency on fossil fuels.

Finances for the typical company in the Power Industry are average, at best.

In addition to the incentives provided by the federal government, many "blue states", such as New York and California, offer additional subsidies.

Some stocks in the industry have not fared well in 2023. Conservative investors may not find these companies suitable.

Recent Developments

Fourth-quarter earnings in the Power Industry were mixed. They ranged from an unexpected profit posted by *Northland Power*, which has been focusing more on offshore windfarms, to a loss from solar power giant and Wall Street favorite, *First Solar*. Results produced by the group's two rock stars,(*Enphase Energy* and *SolarEdge Technology*), were also unexpected. Both of these entities make inverters used in the process of manufacturing solar power. This is the one part of the Industry that has been very successful because the items made are highly-engineered, and not commodity-type product, such as solar panels.

By market capitalization, the sector is dominated by five large corporation (*Enphase*, *Constellation Energy*, *First Solar*, *SolarEdge*, and *AES Corp*). Ironically, these firms are a good representation of the group because there are major differences among almost all of them. While the inverter companies are not too different, *AES* produces most of its power using coal. *Constellation* is a relatively new entity that was created last year when it was spun off from Excel Corp. The company considers itself to be the largest provider of clean energy in the nation.

Future Prospects

Alternative power companies were provided a huge boost last August when the Inflation Reduction Act was passed by Congress. Approximately 85% of $440 billion is supposed to be used to promote the use of nonpolluting power sources. Many of the stocks in the segment were given a boost on the news. However, certain investors did not realize that there will be a lag before this money works its way through the system. Most of the funds are being provided via investment tax credits (ITCs). Hence, we do not see these incentives really kicking in until later in 2023. So, income statements here may not really benefit until 2024.

Mediocre Finances

Over the past half decade, the stocks in this group have underperformed. When oil prices slumped to record lows, the price of alternative energy became very uncompetitive. Certain companies, in addition to incurring substantial losses, were forced to write down the value of assets, too. Thus, today many in the Industry have overleveraged balance sheets. This could be more of a negative should interest rates remain high when it comes time to refinance maturing debt. When rates were low, a few companies were able to issue convertible bonds at incredibly low rates.

Conclusion

Some investors may consider purchasing an industry-related ETF to gain exposure to this space. This could reduce the risk involved, as a bundle of these equities would diversify some of the uncertainty. There are a few timely equities here, but we caution subscribers that the green energy group has been one of the most volatile in the entire stock market. There is a possibility, though, that these equities may finally be entering an era of sustained profitability. Still, this wouldn't be possible without the government's help. Technology has come a long way in this segment, and some breakthroughs could end up making them more price competitive. One scenario of these stocks performing well would be if energy prices spiked while power produced by sources other than fossil fuels continued to get cheaper.

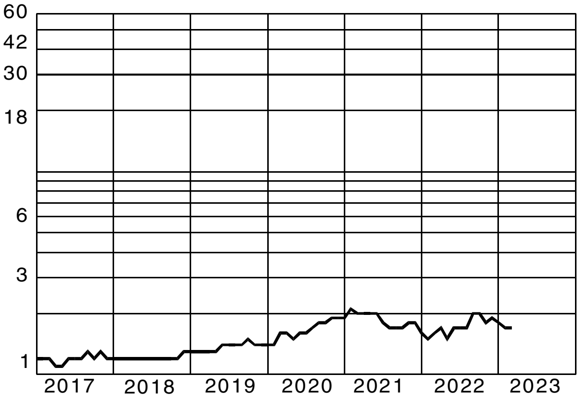
Currently, the stock that offers the best long-term potential here remains *Generac Holdings*.

For investors wanting to take a deep dive into this sector, we recommend the *Value Line Climate Change* product, as it is focused specifically on this market.

James A. Flood

Power

RELATIVE STRENGTH (Ratio of Industry to Value Line Comp.)



Index: June, 1967 = 100