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dialogues



CO-INVESTMENTS: *the* fourth pillar *of* incentives

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DC flows into real estate solutions

NAREIM spoke with *Clarion Partners*, *JPMorgan Asset Management*, *PGIM Real Estate* and *Principal Real Estate Investors* to get a real-time pulse of the DC market, as well as to understand DC real estate appetite in times of market stress and manager considerations surrounding liquidity and rebalancing.

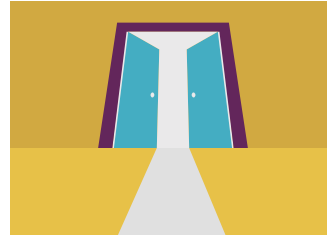
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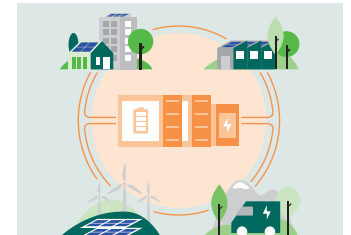
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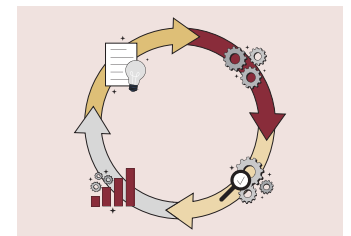
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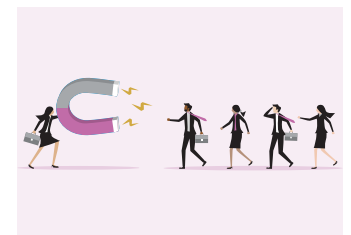


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It's time to POWER up

As the energy industry transitions to renewable sources, the real estate sector can participate in the growing battery energy storage sector through several interesting plays.



By Deborah Smith,
The CenterCap Group

¹ Max Schoenfisch and Amrita Dasgupta, *Grid-scale storage tracking report*, International Energy Agency, September 2022.

² Suparna Ray, *US battery storage capacity will increase significantly by 2025*, US Energy Information Administration, December 8, 2022.

Battery energy storage is a critical component in the world's move towards renewable energy supply. With this shifting focus, the real estate industry could find yet another market opportunity — one that sits at the intersection of real estate and infrastructure.

Before we get into growth in battery energy storage, it is worth understanding how electricity supply and delivery are changing. For the past century, most electricity was produced in large, fossil fuel power plants that operated 24/7. Energy supply from wind, solar and other renewable sources was irregular, intermittent and hard to predict, which limited their economic usefulness. Supply could only reliably meet demand with fossil-based generation.

But in a world that is increasingly electrified (including a surge in electric vehicles that need charging) and focused on renewable energy, change has become necessary. Enter battery energy storage. Large-scale battery systems, together with sophisticated software required for coordination and control, connect to the electricity grid; they charge batteries when supply is plentiful and discharge electricity when demand is high.

Storage owner/operators, operating in organized markets as a merchant, can use a buy low, sell high strategy. Or they can hedge the price and guarantee the supply of electricity for specific facilities, including as emergency backup.

The market opportunity

Battery storage is here to stay. According to the International Energy Agency (IEA), a “rapid scale-up of energy storage is critical to meet flexibility needs in a decarbonized electricity system” and

The physicality of batteries and battery storage facilities

Energy storage batteries are like Legos — they are modular and come in all shapes and sizes. Storage facilities also include the power control system (an inverter and equipment to connect the batteries to the grid), the energy management system (software and communications equipment to monitor and control the batteries), and the balance of the plant (enclosure, heating/cooling infrastructure, fire protection systems).

Modern battery storage systems are turnkey and are easy to install and maintain. They can be connected into the transmission or distribution system, including advantageous locations close to variable renewable facilities or close to sources of demand. As an example, Florida Power & Light and NextEra Energy built a battery storage facility in the urban Miami neighborhood of Wynwood. The facility can discharge 10 MW of energy per hour for up to 4 hours, enough to power about 7,000 homes. It has the size and look of a normal building.

Smaller battery systems — individual modules often about the size of a shipping container — are most common. Unlike cell towers which can be a visual eyesore, battery infrastructure can be made to fit in with neighboring buildings or can be landscaped to go unnoticed. Their noise level is similar to a commercial structure's HVAC unit.

investment in battery storage grew by almost 60% in 2021, reaching close to \$10 billion.¹ The US Inflation Reduction Act provides for more than \$369 billion in funding for clean technologies, which, according to Bloomberg New Energy Finance, will help drive the energy storage buildout. While negligible prior to 2020, the US Energy Information Administration (EIA) expects battery capacity to increase by 20.8 GW between 2023 and 2025.²

Battery storage has found its place in the electricity supply sector, and in helping create a cheaper, greener and more ESG-friendly world.

The real estate play

At a basic level, battery storage is like another familiar asset class — data centers. Akin to data centers storing information, battery storage stores energy. But, dig a little deeper, where does an operator locate battery storage

units? That's where the real estate angle comes into play. There are several ways to look at the opportunity.

1. The first is a land acquisition play. For investors and fund managers who have typically been reluctant to land bank or acquire land without a specified purpose, battery storage offers a new purpose.

The land required is different because it is its proximity to the right location on the grid — where it will have the easiest and cheapest access to energy sources and uses — that matters. This is not a typical approach to how a real estate investor would assess end-use.

These sites do not represent an alternative use of land, but rather an additional use for land that may otherwise be viewed as unattractive, like a backlot, for example. These are sites that real estate owners do not typically put at the top of their location lists.

Interestingly, the right locations are also changing because of changes and trends in electricity use: converting a large fleet of delivery trucks from diesel to electric, for example, creates demand in a new location. Think about it as a potential covered land play where an independent power producer (IPP) seeks entitlement.

2. Battery storage provides for an alternative use of a pad or excess land as part of a larger project. This presents a very different, viable option beyond a Walgreens, Chick-fil-A or Wells Fargo ATM branch.

Battery storage creates a stable and noncyclical source of long-term income for underutilized or repurposed land. This is a new way of making the most of every inch of land. Potential revenue streams include option premiums, long-term lease rents and potential for the appreciation of land value.

3. The third opportunity is one where battery storage facilities bring additional benefits to the primary use of the development.

For example, a battery storage facility adjacent to an industrial facility, shopping mall or office building may offset energy costs for owners/tenants. An industrial facility or hospital campus may utilize a microgrid setup where storage capacity is typically sold into the grid, but could be used internally as emergency backup power if needed.

In addition, as institutional investors implement ESG and net-zero carbon targets, investment in projects that include components that contribute to decarbonization will become important. A project that

includes battery storage may help a project fit that bill.

Let's sketch out a sample business plan. An industrial property owner has a few extra acres of land beyond warehouses. The building owner leases a connection to the battery storage site to an IPP, charging a flat fee and participating in any upside that the IPP creates (think net lease or ground lease). The IPP trades electricity using battery storage to take advantage of pricing arbitrage. A real estate investor could buy (or leverage existing owned) sites and then partner with an IPP whose job it is to get approvals, build the battery storage facilities, undertake the development and hook it up to the grid.

A new, new way of making money

There are a number of existing partnerships between independent energy companies and real estate investment managers/owners/operators. Stream Realty Partners is partnering with independent power producer Catalyze to deploy solar and battery storage projects across its industrial property portfolio. Trammell Crow Company and Altus Power have announced a strategic partnership to bring clean electrification solutions to TCC's real estate development projects. In the initial plan, Altus Power brings solar, battery storage and charging stations to TCC's 35 million square feet of industrial assets. NorthBridge Partners and Green Bridge Energy have formed a strategic venture NetZero Logistics Inc. to invest in energy transition infrastructure for the logistics real estate sector. Then there is BlackRock, which in the last 12 months announced a partnership with UK-based KX Power,

and the acquisition of Australian-based Akaysha Energy. BlackRock announced both deals were focused on developing battery storage assets, with the latter announcement coming with a A\$1 billion (\$700 million) commitment.

Others are tackling battery storage from indoors. LBA Realty's Park Place project, in Irvine, California, which at the time of announcement was held to be the largest indoor battery storage system in the world, has the capacity to store 1.3 MW. The project delivers automated electricity savings to Park Place while also providing on-call demand reduction to help Southern California Edison balance the grid during peak times. The intelligent tech-driven storage system is set to automate energy by directing batteries to store power when energy costs are low, then deploy it in peak times to keep prices down and add stability to energy pricing — all without impacting tenant comfort or operations.

Conclusion

We have seen how the real estate sector responded to the pandemic, from last-mile logistics to cold storage generation, converting, repurposing and reimagining how space can be used. There is now an opportunity to respond to the support for renewables and the desire to cut carbon emissions. It's an emerging niche product called battery energy storage. Battery storage sits at the intersection of real estate and infrastructure, bringing two giant sectors together; and the best part is, it's just getting started. ♦

Deborah Smith is Co-founder and CEO of The CenterCap Group.