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Renewable energy stocks had a record year — here's what Wall Street sees for 2021

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Pippa Stevens
@PIPPASTEVENS13

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Arrays of photovoltaic solar panels are seen at the Tenaska Imperial Solar Energy Center South in this aerial photo taken over El Centro, California, U.S., May 29, 2020. Picture taken with a drone.

Bing Guan | Reuters

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Companies focused on renewable energy are on track for a stellar year in 2020, as attractive economics and growing investor interest in the space pushed stocks to record

The numbers are eye-popping: Enphase Energy is up 594%, while SunPower has advanced 484%. Sunrun is up nearly 400%, while Sunnova has gained 310%.

And then of course there's Tesla, which has gained 690%, while fellow electric vehicle company Nio has rallied more than 1,000%.

Given these sky-high returns — the S&P 500 is up just 14.6% for the year, after all — investors might feel they've missed out on the record rally in renewable energy.

But Wall Street analysts say that even if 2021 won't provide the same stratospheric returns as 2020, there's still plenty of upside left for these stocks.

President-elect Joe Biden has made slowing climate change a priority, which should spur ever-growing demand for alternative energy. And with solar now the cheapest new source of power in many places, the pace of adoption is expected to accelerate.

The rise of ESG investing, or strategies that consider a company's environmental, social and governance metrics, has brought additional attention to the space.

This supportive backdrop comes as technological innovations and economies of scale have made renewable energy systems better and cheaper.

Green infrastructure investments will drive between $1 trillion and $2 trillion in spending each year over the next decade, with the total addressable market for alternative energy doubling in size by 2030, according to Goldman Sachs.

"We look for growth in Alt Energy to accelerate in 2021 as economic merit-based growth is potentially stimulated by more aggressive government support," JPMorgan said in a recent note to clients.

"We have covered the Sustainability sector for 15 years and have never seen the fundamentals any better," added Cowen's Jeffrey Osborne.

But analysts say investors should be picky, focusing on high-quality names that have attractive risk vs. reward profiles. Here are some of the Street's top picks for 2021:

Residential solar is growing at a record pace, but the number of households across the country that sport rooftop panels stands at just 3%, according to JPMorgan. That translates to huge growth potential for some of the industry's top players, especially as natural disasters and frequent blackouts demonstrate the need for greater grid resiliency.

Within the industry, Wall Street analysts say Sunrun and Sunnova stand out.

JPMorgan recently called the two residential solar installers top picks for U.S. growth investors, and the firm has an overweight rating on each one.

"We look for both RUN's and NOVA's profitability to accelerate in 2021 owing to installation volume growth, declining customer acquisition costs (digital sales and permitting), declining cost of capital, increasing attach rates of solar+storage, and ramping cash flow from grid services contracts," the firm wrote in a note to clients.

Each stock has more than tripled this year under the Trump administration, and a Biden presidency should further fuel growth.

In fact there's bipartisan consensus when it comes to many solar issues, and the latest stimulus package passed by Congress includes an extension of the Investment Tax Credit. The credit has been instrumental to the growth of renewables in the U.S. President Donald Trump has not yet signed the bill into law, however.

Within the solar ecosystem, Bank of America also prefers the installers, pointing to accelerating customer growth into 2021, as well as refinancing opportunities and customer value beyond initial contracts.

Between Sunrun and Sunnova, both of which the firm rates as "buy," analyst Julien Dumoulin-Smith said he has a growing preference for Sunrun. The stock has underperformed since closing its acquisition of Vivint Solar in early October, which could be the result, in part, of long-term shareholders trimming positions after the stock's big return.

Hannon Armstrong

Hannon Armstrong, which finances carbon reducing and clean-energy projects, is also at the top of analysts' 2021 lists, despite the stock's near 100% gain this year.

The rise of ESG investing has played directly into the company's dramatic growth.

"Hannon Armstrong checks every ESG box," noted Jenny Harrington, CEO of Gilman Hill Asset Management. "It's the only publicly traded pure play in clean/green energy project financing," added Harrington, who's owned the stock since 2013.

Heading into 2021, analysts at Cowen called Hannon Armstrong one of their top picks.

The firm said that the hunt for yield paired with the company's focus on sustainability should continue to fuel investor interest in the name.

"Hannon Armstrong remains our top idea due to the company's flexible business model and strong moat in niche sustainable finance markets," analysts led by Jeffrey Osborne wrote in a note to clients.

The company currently has more than $6 billion in managed assets. Examples of investments include a public-private partnership to operate, maintain and upgrade the University of Iowa's energy and water utilities infrastructure with sustainability objectives in mind.

Bank of America, which also called Hannon Armstrong a top pick for 2021, noted that yields for renewable financing should remain in the 7% to 8% area, even in a low-rate environment. Analyst Julien Dumoulin-Smith added that even if yields are compressed in certain areas of the market, he could see Hannon Armstrong "transition into new investable markets in order to sustain yields near current levels."

Enphase Energy

Shares of Enphase Energy have rallied nearly 600% this year, but Wall Street analysts say that the company's dominant position in the microinverter market should continue to drive upside next year. Additionally, the company has expanded into home monitoring offerings, as well as the quickly-growing energy storage market.

Piper Sandler recently initiated coverage on the stock with an overweight rating, saying there's momentum behind the company given its robust revenue and free cash flow growth. The firm pointed to four key areas that should boost Enphase's bottom line: Continued market share gains in both the U.S. and European residential markets, as well as its entry into the small commercial market and energy storage spheres.

After Enphase's eye-popping run this year, the stock now trades at 143 times forward estimates, according to FactSet. But JPMorgan believes the valuation remains attractive on a growth-adjusted basis.

"ENPH is one of the few solar stocks that is consistently profitable, generates cash, and has a solid balance sheet," analyst Paul Coster wrote in a note to clients. "We believe that further penetration of the global solar market, and growth from expansion into new verticals, should allow the stock to outperform our coverage over time."

JPMorgan's bullish case centers on positive momentum both for Enphase Energy itself as well as the broader solar sector. The company-specific growth drivers include new products, improving margins and cash flow, as well as international expansion opportunities.

- CNBC's Michael Bloom contributed reporting.

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