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2005 INVESTMENT OUTLOOK -- THE BEST PLAYS

Alternative Energy Gets Real

Pricey oil and gas are heating up industrial interest in renewable sources

Renewable energy is booming. The use of solar power has been growing by more than 30% a year and, except for a hiccup in 2004 -- when Congress delayed renewing a tax credit -- so has wind power. Ethanol is heading for record production levels. And there's no end in sight, given high oil and gas prices, an increasing number of government mandates and incentives, and the first real steps toward tackling global warming. Clean Edge Inc., a research and strategy consultant, predicts that the total clean-energy market will grow to \$92 billion by 2013, about seven times its current size of \$13 billion. "The investment community is starting to see real opportunities," says Ron Pernick, co-founder of Clean Edge.

But buyer beware: Many of the leading companies supplying the technology to produce renewable energy still aren't profitable. Often the pros are divided on just which are the leading companies. In fact, today's renewable business is reminiscent of the computer industry in the early 1980s, "when no one knew who the winners would be," says Carsten Henningsen, chairman of Portfolio 21, a mutual fund that invests in environmentally conscious companies. That's why many analysts and fund managers recommend investing in a basket of companies. "People should try to pick companies positioned to be winners and get enough of them," says Henningsen.

Wind might produce the biggest winners. A U.S. tax credit of 1.8 cents per kilowatt-hour is in place until 2006, and 19 states now require electricity producers

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to generate part of their power from green sources. Energy information and services company Platts, like *BusinessWeek* part of The McGraw-Hill Companies (**MHP**), expects that most of the new sources will be wind. One beneficiary could be Denmark's Vestas Wind Systems, the world's biggest turbine manufacturer, which is listed in Copenhagen and trades over the counter in the U.S. "It is profitable, and there is more certainty and a more favorable political climate surrounding wind than solar or hydrogen," says Henningsen.

Fuel-cell companies are also catching the eye of investors. Their stocks are way down from the speculative peaks of a few years ago, but their products are finally becoming a compelling alternative to diesel-powered backup generators, says Walter Nasdeo, managing director of New York-based Ardour Capital Investments LLC. And they hold the promise of clean, efficient, hydrogen-powered cars, provided costs come down. Nasdeo is bullish on FuelCell Energy Inc., which he expects to reach \$17.50 in a year, from \$8.45 now.

A buy-and-hold strategy combined with some selective trading may be the best strategy for cashing in on the alternative-energy boom. "If [FuelCell Energy] goes to \$14 or \$15, you should take a little profit, then wait until [it] pulls back and buy some more," says Nasdeo. Eventually, he expects one of the renewable energy stocks to hit it big. In addition to FuelCell Energy, Nasdeo sees potential in Evergreen Solar (**ESLR**), which makes solar cells; American Superconductor (**AMSC**), which makes highly efficient superconducting wire and power-regulation devices; and two other fuel-cell makers, Hydrogenics (**HYGS**) and Plug Power (**PLUG**).

Portfolio 21's Henningsen also sees opportunities now to buy companies with beaten-down stocks. His own holdings: Vestas; fuel-cell makers Ballard Power Systems and Plug Power; and IMPCO Technologies (**IMCO**), which focuses on devices for car engines that use alternative fuels. After a fall for these stocks in 2004, "now may be the time to buy," he says.

If investors don't have the time or stomach to juggle a portfolio of individual stocks, they could buy into a fund that specializes in renewable-energy stocks. An interesting choice is the WilderHill Clean Energy Index, set to debut in early 2005. It's the brainchild of Robert J. Wilder, who put together an index of clean energy stocks five years ago as a hobby. It now includes everything from fuel-cell companies to suppliers of carbon fiber for turbine blades and makers of hydrogen. The index soared during the tech boom, plunged, and is now up 26% since August. "There are about 40 representative stocks -- and any one of them might do well," says Wilder. In other words, with a big enough basket, renewable energy could charge up any portfolio.

By John Carey

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