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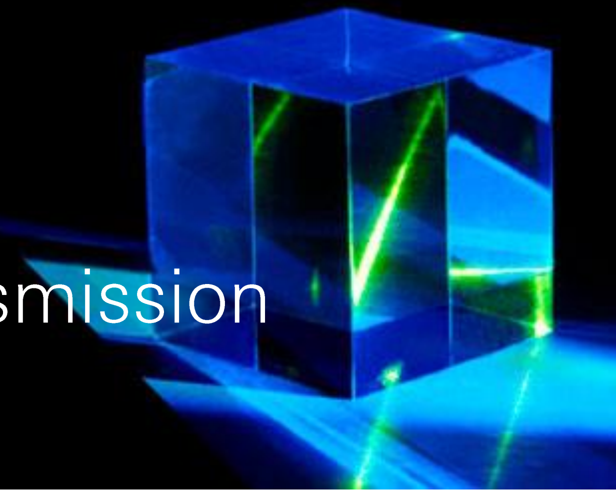

Tariffs, Taxes, President Trump and Transmission

July 2025

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Executive summary:

It has been a busy start to the year for global financial markets with no shortage of significant catalysts emanating from the United States. Geopolitical developments have attracted headlines around the world and driven macro sentiment, whilst there has also been no shortage of political matters impacting domestic sectors and stocks. The back and forth on tariffs, the budget reconciliation bill (or "the One Big Beautiful Bill"), and the steady stream of Executive Orders from the President have all caught investors' attention. State politics has also been particularly active ahead of several key elections this year and next; pursuing economic growth and dealing with cost-of-living pressures important areas of focus for most. The rapid expansion of the data centre industry is in some ways related to these efforts and continues despite the concerns from the Deepseek announcement in Mar-25. Despite this the buildout continues and has been so significant that data centre construction added 1% of growth to the world's largest economy in the first quarter of 2025[1].

These topics have all been important for the profitability and outlook of the US utilities that we follow and invest and it was in this environment that we travelled to the US in 2Q25. Our discussions with those in the industry covered the implications of these issues and more, at a time when many were still evolving. The conversations were also in the context of the evolving energy transition involving topics addressed in our 2022 energy transition thought piece, specifically in relation to gas and nuclear. Similarly, the increasing focus on affordability and the challenges from different drivers of power bills were called out in our paper from last year on the same topic. Whilst the quickly evolving data centre industry and its impact on power demand remains a key theme, as we analysed in our report of a few months ago. We provide below some of our feedback on these topics and others as we continue to closely follow developments for the analysis of our investments in the sector.

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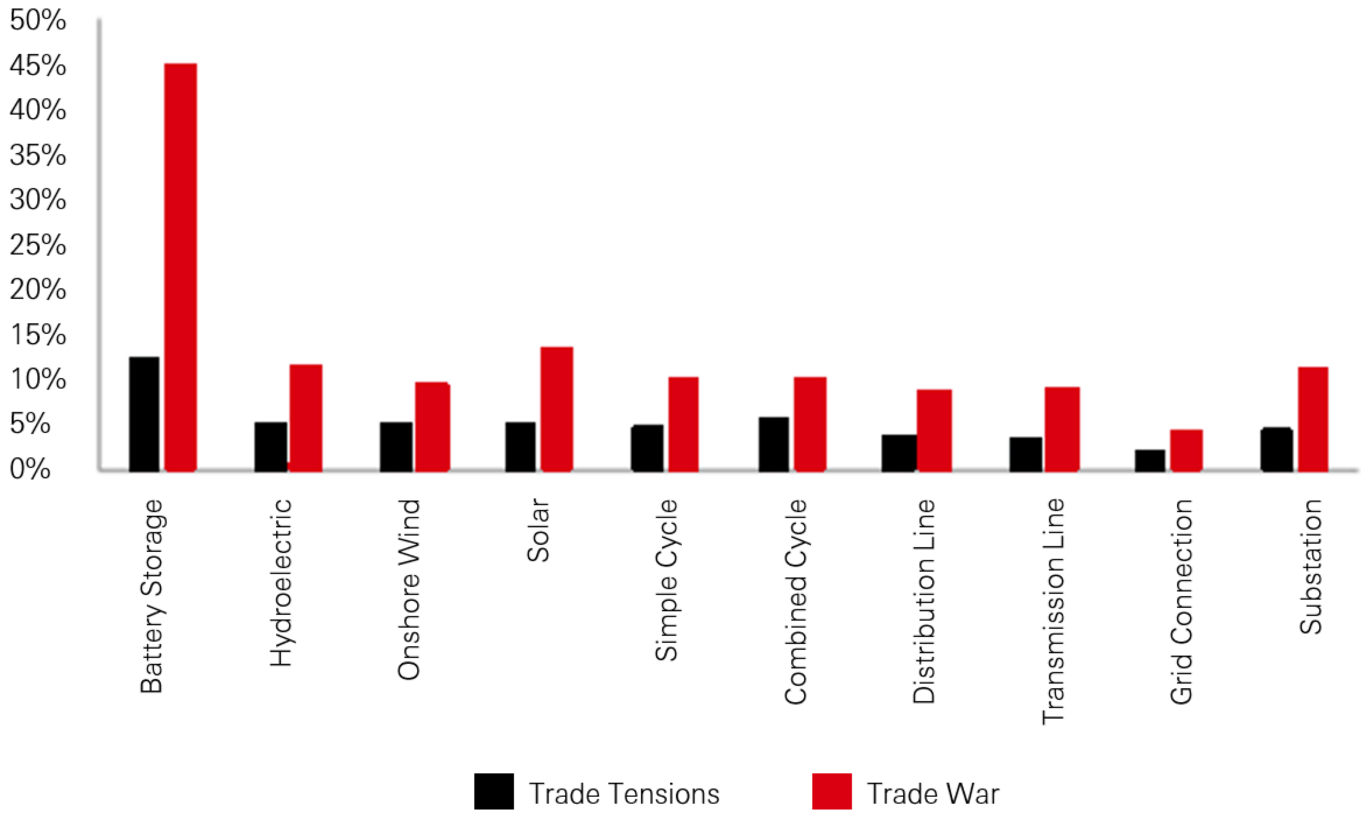
[1] Apollo, 2025

Tariffs have had limited direct impact to the sector, but potentially longer-term implications

The new Administration's focus on tariffs as a policy tool has received a lot of attention from the media and markets so far in 2025. However, it wasn't until utility management teams addressed investors with their 1Q25 results that we formally heard of the expected financial impact. Given labour is the main component of operating expenses for utilities the impact to procurement was more of a capital item, and most companies provided a range that fell within 2–5% of their long-term (4–5 years) capex plans. These levels (at that time) are very manageable for our companies, resulting in either a little more bill inflation for customers or potentially the deferral of less-critical projects.

Feedback from many management teams was that they had been focused on their supply chain strategies in advance of the various announcements from the President and the expected increases could yet be managed lower. Indeed, policies implemented by the previous Administration had incentivised re-shoring of manufacturing, supporting the potential for increased domestic supplies. For US utilities with cost of service-based regulation the extent to which materials can't be procured at prices and quality that differ to international standards is a potential risk borne by the customer and will require further monitoring. Batteries are a good example of this where the domestic industry in the US is at the early stages of development and a technology that will clearly be in increasing demand going forward given the recent build-out of renewables and expectations for the future.

Chart 1: Expected impact of tariff scenarios on utility construction costs (Wood Mackenzie, 2025)



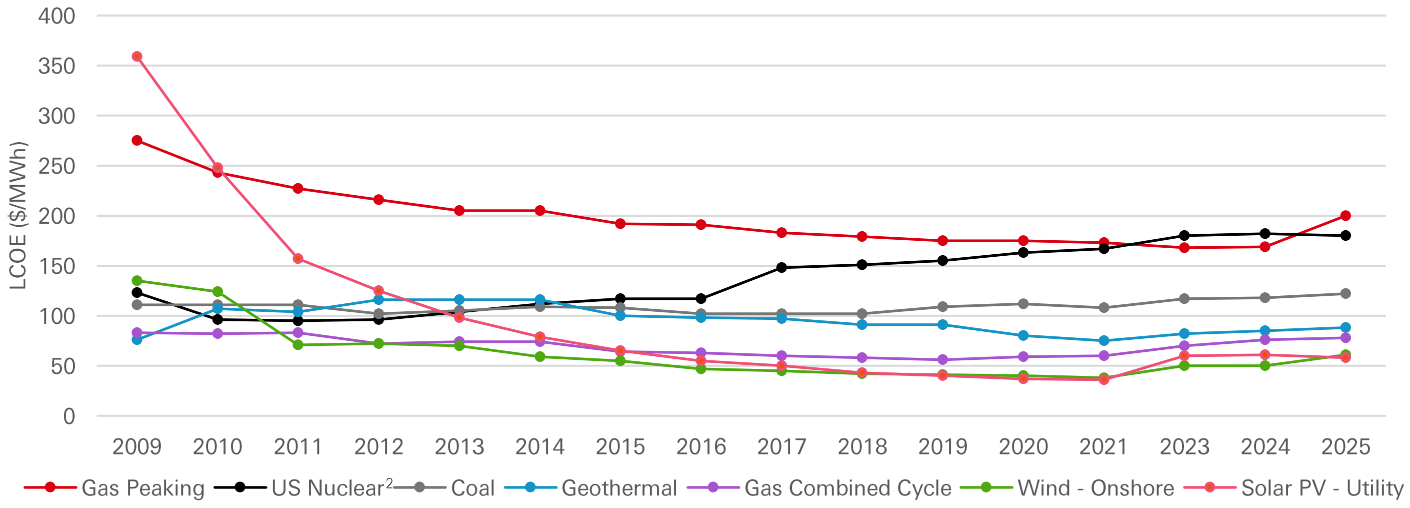
OBBBA repeal of IRA level tax credits is the main focus for utilities

During the pause in implementation of tariffs beyond the 10% baseline, attention turned to the Republican party's One Big Beautiful Bill (OBBBA) initiative. A budget reconciliation bill, the OBBBA effectively implements policy with regards to the federal budget. Following rhetoric during the election campaign, tax credits for renewables and other technologies that were introduced or extended under the previous Administration's Inflation Reduction Act (IRA) were expected to come under close scrutiny and potentially repealed in some way. However, despite the strong language towards renewables from the President this was less straight forward than it seemed given Republican states disproportionally benefited from investments that flowed from the IRA.[2] As a result, this was one of the more contentious areas of the bill, resulting in much back and forth within the party around different versions of a phaseout.

The final legislation provides for tax credits for renewables projects commencing construction within 12 months of OBBBA enactment or in service by the end of 2027. However, safe harbouring provisions are expected to still apply such that projects that have commenced construction will still be eligible for credits if completed within 4 years. The perspective from a lot of utilities was that this was better than originally feared and supportive of their publicly stated capex plans (usually 4–5 years), significant, given these projects form a meaningful component for many. However, management teams acknowledged the lost credits thereafter would increase the cost of renewable generation, which would eventually be incorporated into their regularly updated longer-term resource plans. Even so, renewables are expected to remain the cheapest incremental resource – and the fastest to market with a current shortage of gas turbines – such that the additional expense from the lost tax credits will be borne by the consumer.

Meanwhile, amongst the other tax credits introduced by the IRA those for nuclear have been retained to the original 2032 expiry, an important development for those assets and the potential for new nuclear capacity. This was well-received by owners of nuclear generation, including many utilities, even if not significant enough by itself to encourage investment beyond the optimisation of existing assets. Tax credits for battery storage were also spared from the repeal efforts, an important potential offset for any tariff implications.

Chart 2: Levelised Cost of Energy (LCOE) evolution (Lazard, 2025)



[2] E2, 2024

President Trump's EO's not directly impactful but bare monitoring

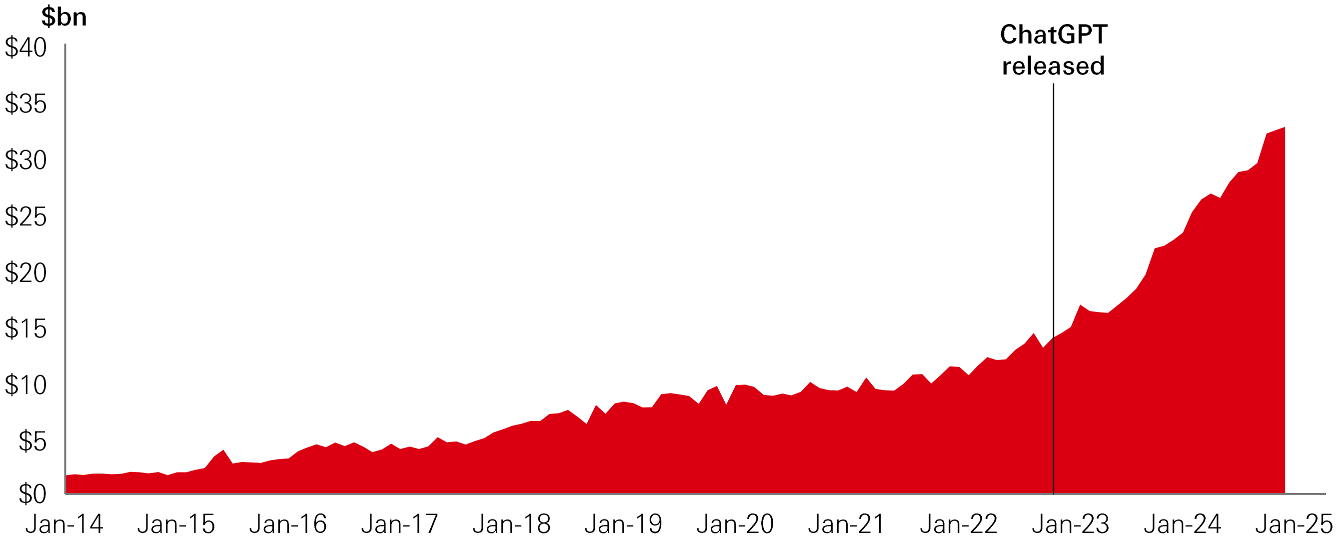
The President has also been active directing policy via a plethora of Executive Orders (EO's), several of which have had implications for the utilities sector. Those most notable in this regard were focussed on stimulating development in the nuclear and coal industries, whilst a third looked to check the support for renewables development. All technologies are at very different stages of their life cycle. Coal has been challenged by various environmental regulations and mandates in recent years which has resulted in accelerating retirements and no new build, whilst nuclear has seen something of a resurgence following a period of limited new investment and a focus now on new technologies. Meanwhile renewables have seen rapid growth over a number of years from supportive tax credits, that were extended by the IRA.

The EO's for coal and nuclear were positive for sentiment and include some small "wins" for each industry (e.g. relaxed regulations and faster permitting) but neither are likely to significantly alter the existing trends. However, the view from the utilities sector was that new coal is still very unlikely, however, some retirements will probably get deferred (also a function of security of supply concerns with increasing demand). Whilst for nuclear, utilities are following developments with Small Modular Reactor (SMR) technologies closely, though they remain highly averse to First of a Kind risks and unlikely to be pursued until more established. The EO for renewables was more recent and developments will need to be followed closely as will future policy developments from the President.

Data centres are driving demand growth, whilst impacts on affordability a point of caution

As policy developments dominated the supply side of the discussion, the outlook for demand continues to improve, with data centres remaining a key driver of this growth. Almost all utilities we met with spoke to their improving demand outlook due to different degrees of data centre, electrification and re-shoring/advanced manufacturing growth. Generally, this is a positive dynamic for utilities as the largely fixed costs (particularly from transmission and distribution networks) are shared over a larger customer base and therefore have the effect of lowering bills. However, eventually the additional growth will require further investment, be it on the grid or additional supply, and the extent to which this can be offset by increased revenues from additional demand will determine how positive an outcome it might be for all stakeholders.

Chart 3: US private data centre construction expenditure latest demand growth expectations (US census bureau, 2025)



This has been a notable dynamic from the increased data centre demand, where they bring large loads but pay a significantly lower tariff and may require large investments. For the utilities, balancing these effects such that existing customers don't subsidise new demand has been critical to the success of data centre deals and the support from regulators, politicians and other stakeholders. Where power is sourced from capacity and/or energy markets these circumstances are a little more challenging as a lack of new baseload generation investment in recent years has meant rising demand is putting upwards pressure on prices. These more meaningful price increases have been starting to flow into the pass-through component of utility bills in recent months, which has resulted in the associated media and political attention. Utilities operating in these markets have been sensitive to these pressures and working with regulators to address the affordability concerns, including respite for certain customers and focussing investments where they can potentially help reduce bills.

Affordability and resource adequacy; states governments are poised to respond

The affordability concerns have not been lost on state politicians with many proposing legislation to address these challenges, or pursuing reforms to power markets where pressures have arisen. States in the PJM power capacity market region of the mid-Atlantic have been particularly active with a number proposing legislation for utilities to build regulated generation as a potential solution for the lack of forthcoming new supply. Elsewhere, some states have looked to transfer different cost items from the utility bill to the taxpayer to ease bill pressures, whilst others have focussed on improving the regulatory construct to encourage investment by the utilities (particularly in generation). States more to the west have been no less focussed on affordability but in addition have been dealing with evolving wildfire concerns and looking at ways to limit the risks and liabilities for utilities. Nowhere is this more critical than in California given the impact of the Los Angeles fires in January and the reforms needed for the state's wildfire fund. The legislative session there runs until September and the topic, along with addressing affordability, are being followed closely by the local utilities and investors.

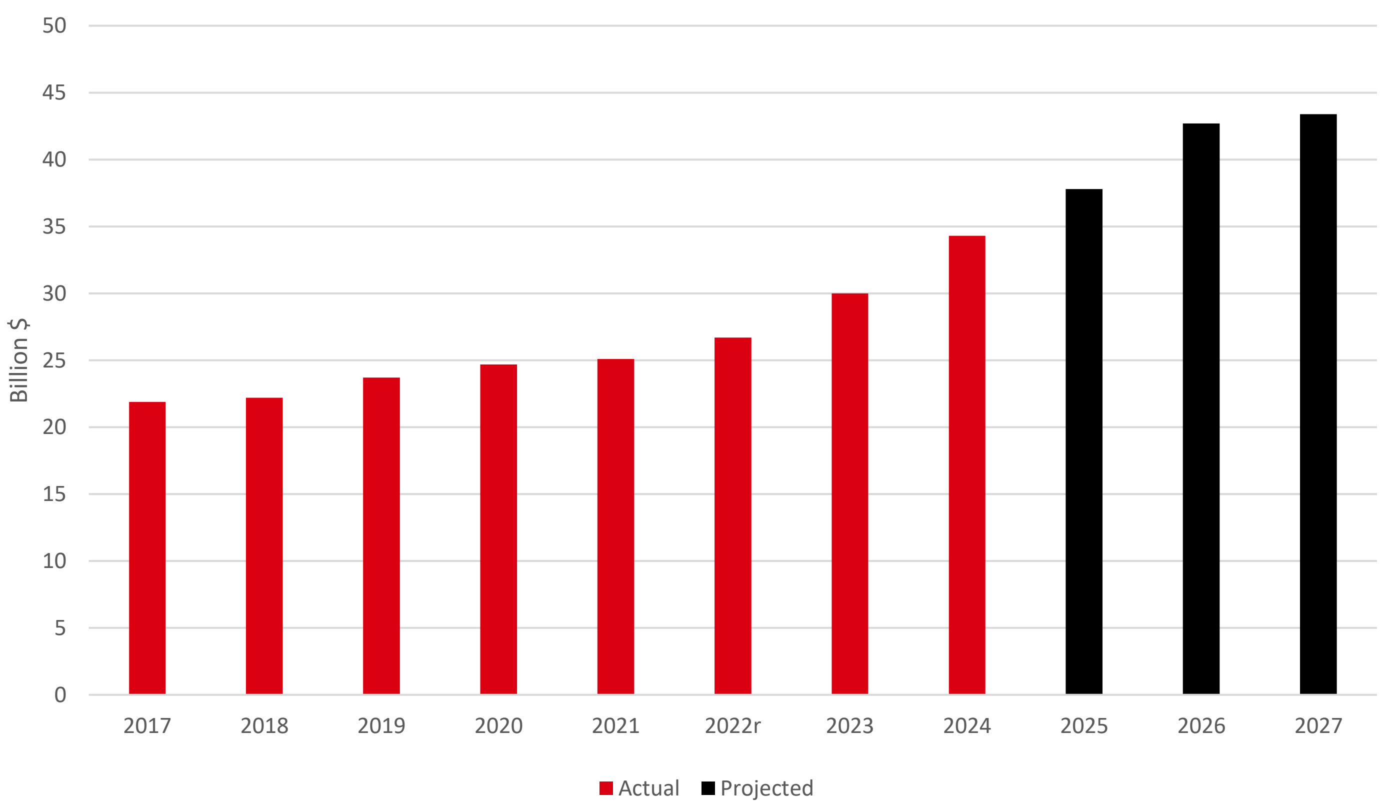
Subject to each state's market structure, regulation, energy policies and other characteristics, all are focussed on affordability concerns, to varying degrees. Similarly, all states have an agenda for economic development and different initiatives to attract investment from different sectors. Waiving state taxes for data centres (and for other sectors) has been a common proposal, amongst other initiatives. Utilities have a role to play here as well given the relative appeal of their rates compared to other states and regions. All utility management teams communicated their active engagement with politicians and stakeholders in this regard, and in general, to improve outcomes for their investors and customers.

Transmission could potentially be part of the solution

It is generally accepted by most utility industry stakeholders in the US that the investor-owned utilities need to be part of the solution to meeting the growing demand with new supply, ensuring reliability, and keeping bills affordable. Utility investments are a key component of addressing this trilemma and despite the associated cost recovery incurred, should lead to lower bills and/or improved service for customers. For the utilities that we are following in the US, transmission investments are expected to play an increasingly important role in this regard, due to both the under-investment for many years and the criticality of connecting supply and demand. These investments could include connecting new large loads (e.g. data centres) where capacity exists, connecting new supply resources (e.g. renewables) to meet demand or improving flows through de-bottlenecking and enhancing reliability (mitigating outages).

Given their importance to the current challenges in the industry there has been a renewed focus on these investments from most stakeholders. However, separate to most other utility investments, transmission is regulated at a federal level (by Federal Energy Regulatory Commission, or FERC), whilst planning is undertaken at a regional level (by Regional Transmission Operators, or RTO's), requiring different levels of engagement. Management teams are closely following developments at the FERC with several relevant topics before the Commission and recent Commissioner appointments by the President. Whilst the various RTO's have developed an almost annual rhythm to allocating projects to the utilities and/or running competitive tenders. Meanwhile the utilities also called out Federal legislation on permitting reform as a further catalyst given the long lead times usually involved with these projects. All are important to what is a potentially high growth segment of the industry.

Chart 4: US investor-owned utility transmission investments (EEI, 2025)



Conclusion

The US utilities sector has seen a busy start to 2025 with no let-up expected for the rest of the year and beyond. State and Federal legislation, Presidential Executive Orders, evolving demand growth (particularly from data centres), affordability and wildfire concerns, have all been topical so far this year and will continue to play out in the months and years ahead. Meanwhile, investment opportunities such as transmission, but also across the industry, continue to evolve favourably. Given the attractive growth at returns that more than compensate for the inherent risk characteristics, we believe it is exciting time to invest in the US utilities sector, and the discussions from these interactions an important input into our investment process. As such, we will continue to closely follow these factors and others for the companies we follow and invest for the benefit of our clients' investment outcomes.

Meet the Author

Joseph Titmus

Managing Principal, Listed Infrastructure Equity
joseph.titmus@hsbc.com.au

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- **Interest rate risk:** As interest rates rise debt securities will fall in value. The value of debt is inversely proportional to interest rate movements.
- **Counterparty risk:** The possibility that the counterparty to a transaction may be unwilling or unable to meet its obligations.
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- **Liquidity risk:** Liquidity risk is the risk that a Fund may encounter difficulties meeting its obligations in respect of financial liabilities that are settled by delivering cash or other financial assets, thereby compromising existing or remaining investors.
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