Customer & Market Due Diligence Of NG LDC Equipment Supplier:
Establishing Natural Gas Consumption Outlook In Light Of Decarbonization

The Challenge: One of our PE client's portfolio companies, a leading North American supplier of equipment serving Natural Gas (NG) Local Distribution Companies (LDCs), was looking to acquire a leading European supplier of similar equipment with a presence in Europe, Middle East, and Asia. While attracted by the opportunity to establish a global presence, our client was concerned about the NG market outlook in light of decarbonization trends and also wanted a fact-based market assessment for a possible exit in 1-2 years. Gotham was retained for a 5-week customer & market due diligence to establish: (1) macro trends in NG usage; (2) market size/growth for the target's equipment; and (3) the target's reputation/competitive positioning.

Global NG Usage Outlook Analysis: Gotham undertook a multi-pronged approach:

- Established historic and projected NG consumption trends by country/state and by sector leveraging data available from government agencies (e.g., EIA, IEA, Eurostat, Statistics Canada); as this data had not yet fully accounted for COVID impact on NG consumption, Gotham established the COVID impact trend and adjusted government projections accordingly.
- Built a country-level market sizing model considering population growth, commercial real estate square footage, and industrial activity to estimate the number of NG distribution endpoints and the NG LDC equipment market size of and growth rate
- Established government regulations, incentives, and utility plans by country in the EU and by state in the U.S. to understand the potential impact of decarbonization on NG consumption
- Conducted interviews with decision-makers (utilities, distributors, competitors, etc.) across Europe and North America to gain insights into: the target's strengths and relationship with its customers; customers' product needs, purchasing process, and supplier selection criteria; NG LDC equipment competitive landscape; number of endpoints; and decarbonization initiatives
- Conducted research to establish NG LDC equipment products, technology, and trends, as well as the overall competitive landscape and profiles of key competitors.

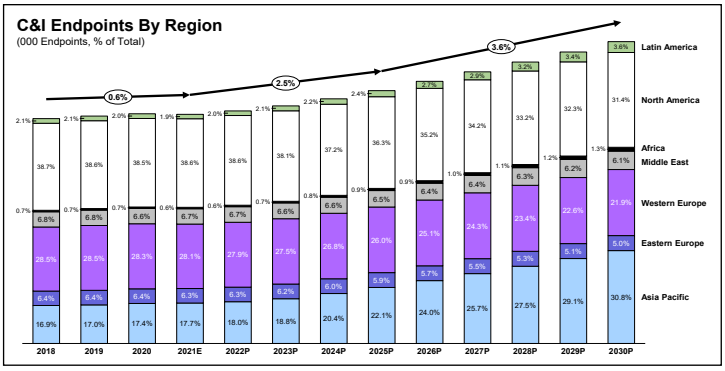
European NG Consumption Expected To Decline At ~1% CAGR With North American Consumption Flattish

As Russia is the primary NG supplier to EU27 (38% in 2019) and NG consumption in EU27 is impacted by supply fluctuations caused by geopolitical tensions, EU27 is diversifying its supply base by increasing import of LNG from other countries. However, NG's importance as a fuel source and the pace of decarbonization varies by country. Germany and Italy are highly reliant on NG while France uses less NG due to an abundance of nuclear power. Netherlands is pursuing decarbonization due to the impending shutdown of the Groningen gas field. While Western European countries are pursuing net-zero emissions, Eastern European countries continue to build out their NG networks. Utilities are pursuing adoption of hydrogen and biogas to utilize their NG network to meet net-zero emissions goals. Biogas has no impact on the use of NG equipment as it is purified to the standard of commercial NG. Hydrogen can be blended up to 20% in existing gas supply without changes to current equipment – hydrogen projects are still in pilot stages, but hydrogen compatibility requirements are already being added to some utility technical specifications.

While 55+ local governments in CA, Seattle, and NYC have added bans on NG connections for new construction, the overall U.S. NG consumption trend has remained positive as other states have prohibited local NG bans. Hydrogen and biogas adoption is at a comparatively early stage in the U.S. While heat pumps are cost-effective and more prevalent in southern states, they are not to generate sufficient heat on extremely cold days and require a high level of insulation. In cold climate regions, utilities are pursuing dual sources to meet net-zero goals where heat pumps provide heat on most days and NG still provides heat on extremely cold days thus not affecting the need for NG LDC equipment. In the industrial sector, NG accounts for ~35% of fuel consumption, with a large part of industrial NG use for high-temperature heating applications unsuitable for electrification.

13.6MM Commercial & Industrial (C&I) Endpoints Globally Expected To Grow 2.5% Through 2025

Asia Pacific endpoints are projected to grow rapidly for the foreseeable future as countries like India build out their gas distribution networks – new connections will account for more than half of the global NG LDC equipment market. Western European endpoints are expected to grow very slowly as decarbonization initiatives start offsetting the oil-to-NG conversions and building growth that is leading the NG LDC equipment market to decline slightly, mainly sustained by the replacement market. North American endpoints will grow slowly, with the NG LDC equipment market flattish (replacement demand 90% of the total).



Target Is A Leader In The NG LDC Equipment Market, With A Reputation For High-quality Products

The target is one of top 2 NG LDC equipment manufacturers, with some smaller specialized suppliers in the mix. While the target maintains a leading position globally, local leaders have established stronger positions in some markets by catering to local needs. Gotham found that the target has a reputation for high-quality products and is viewed as a good partner. Furthermore, customers purchase this equipment through a tender – 2-3-year contracts, volume spread among 2-3 brands. Price, technical specifications, and quality are the top 3 vendor selection criteria, and the target scores well on all 3 of these criteria.

The Outcome: Gotham's data-driven approach allowed our client to gain confidence in the outlook for the global NG market and in the expected future demand for NG LDC equipment and move forward to close the deal.