

Customer & Market Due Diligence Of Fluid Power Equipment Company: Assessing Adjacent Market Opportunities In Several Technically-Complex Niches

The Challenge: Our client, a large PE firm, was considering an investment in a fluid power equipment repair & remanufacturing company, with a strong presence in the underground mining market. The target was projecting its next leg of growth to come from offshore oil & gas market where it had recently gained traction. As the viability of the target's growth in this and other adjacent markets was a key part of our PE client's investment thesis, Gotham was brought in to quickly validate these growth opportunities by pinning down the market and competitive dynamics of each of the adjacent markets under consideration. Our due diligence effort entailed 2 phases: Phase I, ahead of the final round bid, focused on the larger offshore oil & gas market; and, Phase II, during a 30-day exclusivity period, focused on a short-list of additional adjacent markets.

Rapid Niche Market Assessment: Given the niche and technical nature of the markets under consideration, Gotham needed to take a bottom-up, multi-pronged approach to establish the market size/growth rate, competitive dynamics, and technical aspects. Our effort encompassed: 150+ competitor, customer, and other key industry participant interviews; extensive secondary research; government and industry data analysis; robust new and aftermarket market sizing model; and competitor profiling.

Expansion Of Offshore Oil & Gas Activity To Deeper Waters Driving Demand For More Advanced Floating Drill Rigs

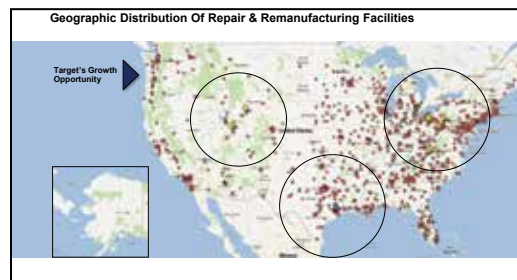
Gotham's profile of oil & gas reserves, production, and drilling activity by region and water depths showed that deepwater production was projected to grow at nearly 10% CAGR. Furthermore, the most favorable long-term growth outlook for deepwater drilling capex was in the waters off Brazil, West Africa, and in the Gulf of Mexico (projected at 10.6%, 9.6%, and 9.0% CAGR, respectively). To understand the impact of this activity on the demand for offshore rigs (e.g., jackups, semi-submersibles, drillships), Gotham analyzed rigs owned by drilling contractors (e.g., Transocean, Seadrill, Diamond Offshore, Sete Brazil), including size of fleet, age/capability/location of each rig, and number of rigs on-order and their delivery schedules. Leveraging this fact base, Gotham established that the market for newbuild offshore drill rigs was mid-way through a strong 10-year demand cycle, with deepwater floaters having the highest demand. Even with costs approaching \$1B, demand for the most advanced ultra-deepwater rigs (floaters capable of drilling at depths >7,500 ft.) was projected to double to 140 in 2013 (vs. 72 in 2010). This growing demand for offshore rigs was driving strong historic and forecasted growth for OEM rig equipment suppliers (e.g., NOV and AKER Solutions).

Target Well-Positioned To Capture Sizeable Share In Its Segment Of The Offshore Oil & Gas Fluid Power Equipment Market
To pin down the target's growth and positioning in the offshore oil & gas fluid power equipment segment, Gotham:

- **Researched and analyzed offshore oil & gas rig equipment technologies** to gain a thorough understanding of the technical details of fluid power equipment. We found a growing demand for more sophisticated equipment, as deeper waters expose rigs to stronger heave due to wave action. With drilling moving to Brazil and West Africa, corrosion dynamics were also changing due to higher salinity and temperature, causing an increase in frequencies of repair and overhaul. The technology was shown to significantly extend equipment useful life vs. other coating options (e.g., PTA weld overlay, chrome plating, ceramic coating).
- **Conducted extensive research on the competitive landscape**, including face-to-face meetings with key competitors to profile competitors and pin down target's positioning. Our research indicated that the target is highly regarded by customers (only one competitor has equivalent technology). Target also has relationships with significant customers, including 2 of the top OEM rig equipment suppliers and 3 of the top 7 offshore drilling contractors (the 7 largest fleets account for 60% of 389 deepwater rigs).
- **Built a fact-based bottom-up market size/growth model** for the target's component segment, triangulating demand driver forecasts from 3 different leading industry sources. To provide a reliable market estimate, Gotham meticulously addressed market complexities, including different equipment types, price structures, technical characteristics, and repair frequency.
- **Estimated that the target was in position to achieve a 25% market share by 2016.**

Beyond Offshore Oil & Gas, Adjacent Market Growth Strategy Requires Targeted Geographic Expansion

With management input and PE client direction, Gotham rapidly analyzed additional end-market opportunities in marine (fishing, cargo, and passenger vessels), forestry, and civil infrastructure (locks & dams, hydropower plants), building a top-down model to project growth outlook in target's product segment of each market. Our assessment indicated these markets were small, with more "commodity-like" applications and longer repair/replacement cycles. Given that these adjacent markets are small and more regional in nature, Gotham recommended that the target pursue a geographically targeted growth strategy in this regard. Based on the regional demand profile for key adjacent end-markets and the target's existing footprint, Gotham identified the Pacific Northwest as the largest opportunity. The team then performed a further deep-dive assessment and targeted interviews of key competitors in that region, shortlisting 10 players as potential acquisition candidates and profiling their facility size, key capabilities, and end-market focus.



The Outcome: Based on Gotham's Phase I due diligence findings in the offshore oil & gas market, our PE client was able to move forward with confidence through the competitive bidding process and obtain a 30-day exclusivity on the target. Gotham's Phase II assessment redirected the client towards a geographic-focused adjacent market growth strategy (in addition to the oil & gas market), enabling them to pursue acquisitions in the Pacific Northwest immediately after closing the deal.