

## Customer & Market Due Diligence Of Water Well Services Provider: Establishing Market Dynamics And Growth Outlook

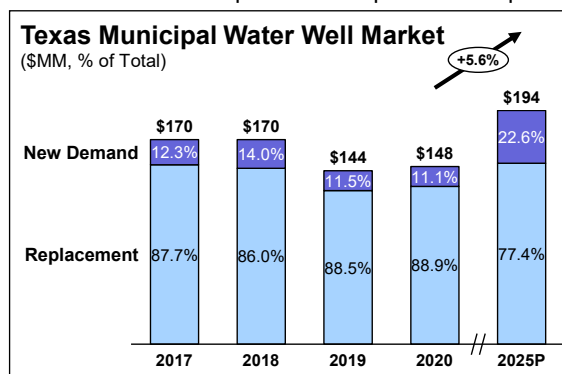
**The Challenge:** One of our PE clients was in exclusive negotiations to acquire a leading provider of water well drilling services for municipal and commercial & industrial (C&I) end-markets. Operating as a family-owned business, the target was serving the water infrastructure need in a growing Texas region and had become a market leader within the eastern half of Texas. Our client was attracted to the target's strong market position as well as opportunities for geographic and service line expansion but first wanted a clear view of the outlook for water well drilling and the target's competitive positioning. Accordingly, the client asked Gotham to conduct a 3-week customer & market due diligence to: (1) establish market dynamics/trends in the target's current and potential expansion markets; (2) establish the target's competitive positioning/reputation; and (3) establish the target's growth opportunities.

**Local Water Infrastructure Services Market Assessment:** To deliver a comprehensive and fact-based view of the market and competitive dynamics, Gotham:

- Analyzed and leveraged water well drilling databases and other available data sources to establish: a detailed inventory of water wells by depth, diameter, end-use, etc.; a water well market sizing model to forecast well drilling by end-market and geography; demand for replacement wells due to aquifer water restrictions; and the recession impact on water well drilling services
- Conducted ~75 warm and anonymous interviews with municipal and C&I water well customers to establish the target's value proposition/competitive positioning and gain insights into: addressable market, including current water well inventory and expected well drilling activity going forward; buying behavior and key performance criteria for selection and evaluation of water well drilling vendors; and water well and pump/motor maintenance needs
- Leveraged information available from government agencies and conducted interviews with water management agencies to: establish water level, compaction, and groundwater withdrawal trends in the target's current and potential expansion geographies; understand environmental regulations and permitting/licensing requirements for drilling and maintenance of municipal and other well types; and evaluate forecasts for population growth and other key factors driving use of municipal water sources.

### Texas Water Well Drilling Market Has Modest Growth Outlook Driven By Aging Wells And Population Growth

The availability and cost of ground vs. surface water drive water well drilling, with Gulf Coast and Carrizo-Wilcox aquifers making the eastern half of Texas a top user of groundwater. Across the state, water resources are managed through multiple agencies and groundwater conservation districts tasked with working closely with water utilities to develop local water plans and to provide local permitting for well drilling. Gotham's market sizing model estimated a ~\$1B market for water well construction in Texas with over 30K water wells drilled annually. Despite accounting for <1% of these constructions, municipal wells represented ~15% of the market as they tend to be deeper and costlier to drill than other wells. Through further analysis, we discovered that 3 regions represented the bulk of Texas' municipal water well drilling, accounting for ~83% of the \$148MM total municipal water well drilling market. This segment of the market also showed strong expected growth at 5.6% CAGR through 2025, largely due to the need for replacement of aging wells, as well as new demand based on water demand growth and water management strategies. Our interviews with municipal customers indicated that municipal well drilling would also have to increase in response to population growth within key regions.



### Target Is Market Leader In One Metro Area With Strength In More Complex Wells

While over 500 companies drill water wells in Texas, competition is quite fragmented and generally local in nature, with each region having its own leader. Companies also tended to serve specific end-markets characterized by varying degrees of well drilling complexity, and only about 8% of companies were currently active in the municipal market, which requires the deepest and most complex wells. The target is one of the top 3 municipal well drilling players in Texas and is able to drill deeper and wider wells than the 2 other key players. Beyond these 3 key players, 6 smaller players were competing in the market, as well as other players with a primary focus in other end-markets. Our interviews with municipal water well customers indicated that the target was the most recognized well driller in its key service areas and was well regarded by its customers, with a high NPS (74) and scoring well on customers' key selection criteria (staff skill level, quality of work, equipment capabilities).

### Multiple Geographic, Service Line, And End-market Expansion Opportunities

Our assessment of potential expansion geographies uncovered two key metro areas with attractive profiles for the target. One region provided the greatest near-term growth opportunity due to the large number of demand-driven wells in the area and the highly-fragmented driller market. The second region showed a moderate installed base of wells with a strong municipal growth outlook. The two regions combined to represent ~47% of the new municipal water well supply by 2040, allowing the target to pursue this growing need that would leverage its core strengths. With heavy C&I water well drilling also within these regions, the target would be able to expand into other high-value end-markets. The target could also leverage its experience servicing water pumps to expand its service line offering. Our customer interviews indicated that along with other maintenance work, pump/motor repairs and well rehabilitation occur approximately every 10 years, giving the target another avenue for accelerating its growth.

**The Outcome:** Gotham's assessment provided reliable clarity on our client's core questions about the target's competitive differentiation within the water well drilling market in Texas and its growth opportunity. Armed with this solid understanding of market dynamics and the target's reputation/competitive positioning, our client was able to pursue the transaction with confidence.