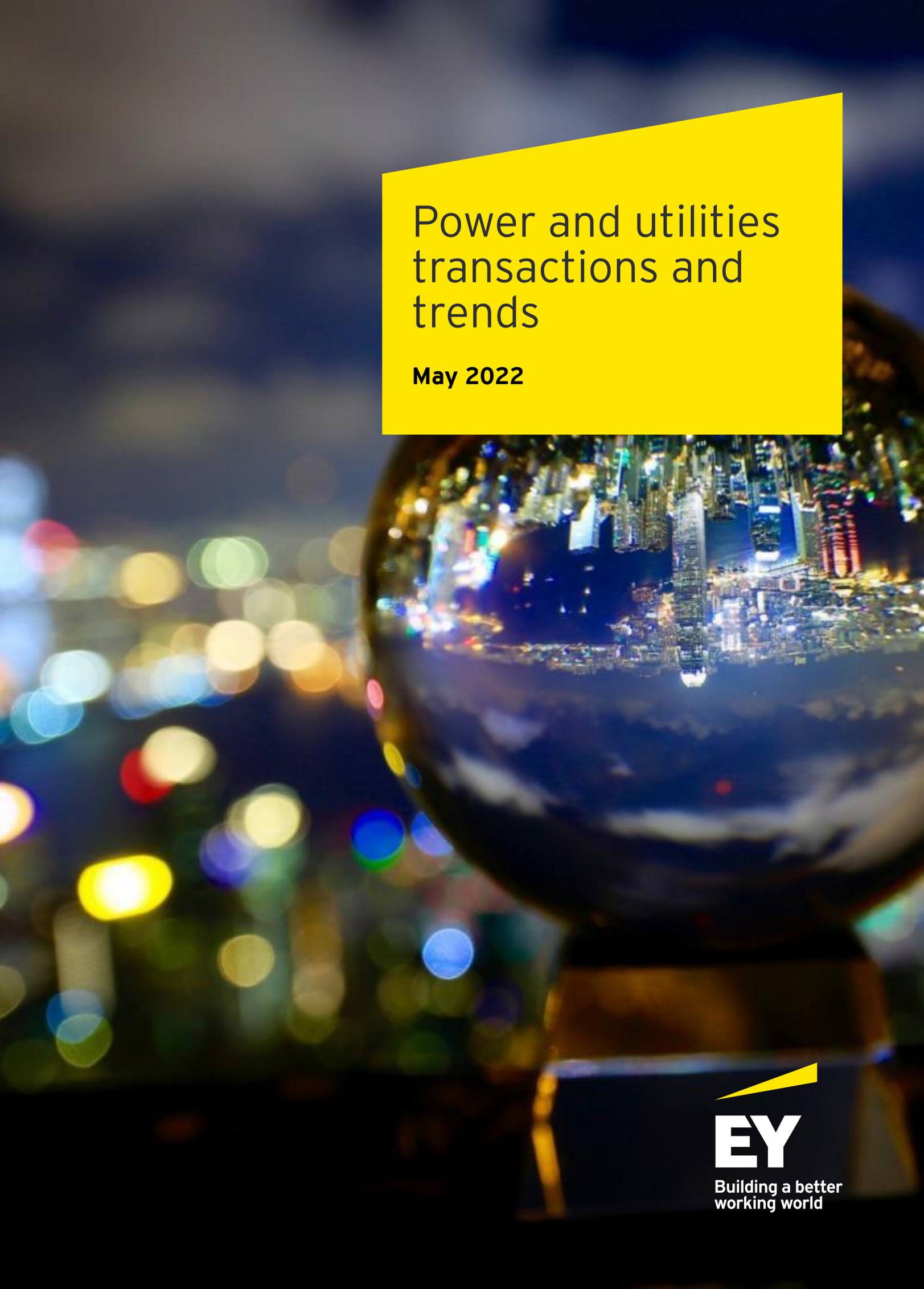
Power and utilities transactions and trends

May 2022



EY

Building a better working world

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Over the past several years, utilities have benefited from low commodity prices to keep supply costs down, giving companies greater flexibility to invest in systems without major rate increases. As nations such as the US are grappling with major challenges, including soaring inflation and commodity prices, stretched supply chains and slowing growth, regulators will be confronted with enduring challenges to achieve affordability of utility rates.

Looking back at deal activity in Q1

The renewable energy and gas utility segments accounted for almost 80% (US$38.5b) of total deal value, primarily driven by financial investors. Renewables witnessed the highest deal activity in terms of both aggregate deal value (US$19.6b) and deal volume (104), however the largest deal of the quarter was the acquisition of a 60% stake in National Grid's UK gas transmission and metering business for US$10.5b by a consortium of infrastructure investors.

US deal value reached the highest in the past eight quarters driven by deal-making in the gas utility segment

The US witnessed deal activity amounting to US$13.2b, the highest since Q1 2020. Within this, 57% (US$7.6b) was driven by the single largest multibillion-dollar deal where Infrastructure Fund agreed to acquire South Jersey Industries at a 46.3% premium. In another interesting deal, Ullico Inc.'s infrastructure fund acquired Hope Gas at 26.2x P/E and 2.0x rate base multiples.

These deals reflect how gas utilities in certain regions continue to be attractive to financial sponsors. Such attractive and lofty valuations have sparked discussions and deal-making expectations in the gas utility segment. However, we note that gas utilities seem to be making a comeback in the public markets, achieving the best performing segment in Q1 with a Total Shareholder Return (TSR) of 13.2% in the Americas. This current favorable public market sentiment is likely to make it more expensive for financial sponsors to continue their shopping spree.

Energy security imperatives continue to boost global energy infrastructure investments

Since late February, the war in Ukraine has cast a shadow over the energy landscape. The European countries' decision to end its reliance on Russian hydrocarbons is without precedent. Also, with other countries imposing bans on Russian oil, coal and gas imports, the energy landscape and trading patterns are being redrawn. Russia's energy hold over European countries is significant. In 2021, EU imported around 45% of its gas from Russia. Through its proposed REPowerEU plan, the EU is aiming to reduce its dependence on Russian gas imports by two-thirds within a year, and phase them out altogether "well before" the end of the decade. Across Europe, new liquefied natural gas (LNG) import capacity and pipelines would be required to source gas from elsewhere. Investors' confidence in the US LNG sector has skyrocketed leading to a race to bring export projects online. This favorable investor sentiment has been supported by US and European leaders' recent announcement of a cooperation plan to help European countries move away from Russian gas supply.
With energy security taking center stage, Germany has said it would invest in LNG regasification terminals while other countries have announced plans to delay closure of some of their nuclear and coal-fired generation. Capital investments in infrastructure are expected. Europe's energy transition is expected to help spur development of alternative sources of energy, including renewables and emerging fuels, such as blue and green hydrogen.

Flight to quality may lead to utilities outperformance in 2022

During periods of macroeconomic cycle turning defensive, utilities have benefitted from strong TSR and valuation, which may be a catalyst for deal making opportunities for achieving economies of scale in operations and bigger balance sheets to drive investments in the structural energy transition while at the same time balancing affordability of utility rates.
We expect continued interest in large and stable companies for higher returns and quality and safe assets. Additionally, financial sponsors will continue to invest aggressively across subsegments in the power and utilities (P&U) sector, including regulated gas businesses and competitive renewable energy platform deals (including wind, solar and hydro assets). Stable earnings growth potential and an accelerated shift toward energy transition is driving the cash-rich infrastructure funds to drive deals.

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Global deals summary

Europe emerged as a hotspot and drove the global deal value to US$49.3b

Total deal value in Q1 2022 amounted to US$49.3b, 19% less than the US$60.9b value in Q4 2021. The number of deals announced in the quarter stood at 160, lowest in the past six quarters. It is notable that almost 80% (US$38.5b) of the deal value was in renewables and gas utility segments, majorly driven by financial investors. The renewables segment witnessed the highest deal activity in terms of both deal value (US$19.6b) and deal volume (104). While the gas utility segment witnessed the second highest deal value of US$18.8b across only three deals.

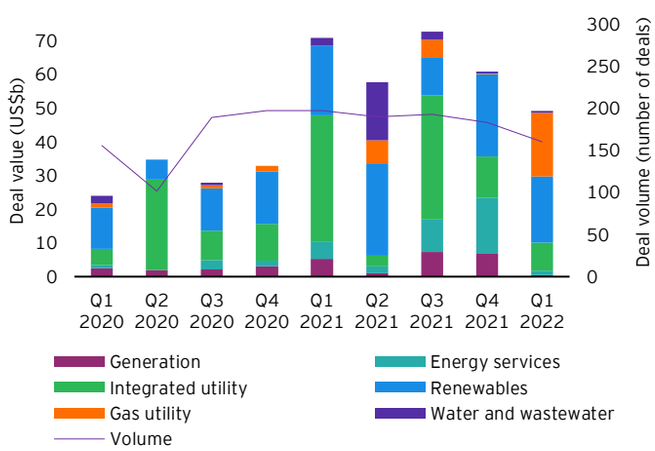
Across regions, Europe emerged as the hotspot of dealmaking activity both as an investment destination and as an investor. In all, 82 deals (51% of total deals) totaling US$22.7b (46% of the total deal value), were completed.

The largest deal of the quarter was National Grid's agreement to sell 60% of its majority stake in its UK gas transmission and metering business to a consortium of long-term infrastructure investors, including Macquarie Asset Management and British Columbia Investment Management Corporation for US$10.5b. The transaction is a part of National Grid's strategic pivot toward electricity and is in continuation to its acquisition of Western Power Distribution in 2021. The deal will increase the proportion of electricity in its portfolio from 60% to 70%.

	Q1 2022	Q1 2021
Global deal value	US$49.3b	US$73.3b
Largest segment	Renewables US$19.7b	Integrated US$37.5b
Largest region	Europe US$22.8b	Europe US$37.2b
Total deals	160	197

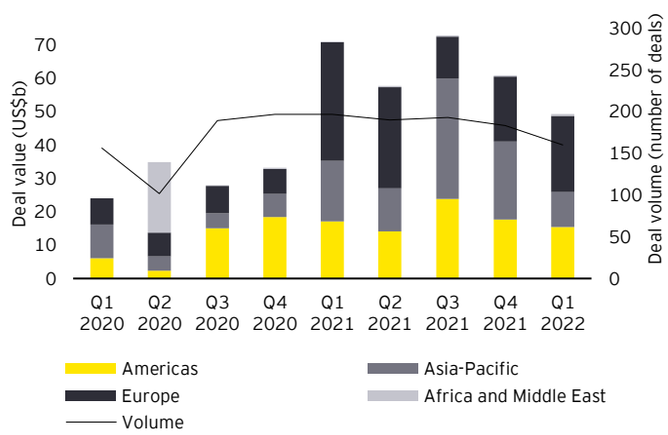
Note: All transaction information is from the EY analysis with data sourced from Mergermarket.

Chart 1: Global P&U deal value by segment
(announced asset and corporate-level deals, Q1 2020–Q1 2022)



Source: EY analysis with data sourced from Mergermarket.

Chart 2: Global P&U deal value and volume by region
(announced asset and corporate-level deals, Q1 2020–Q1 2022)



Source: EY analysis with data sourced from Mergermarket.

Accelerated energy transition dominated the deal activity in Q1 2022

Deals in renewables and gas utility segment dominated the deal value in Q1 amounting to US$38.5b, majorly driven by financial investors.

Constructive energy policy support is needed to attract energy transition investments

In Q1 2022, continued policy support to seek alternatives to fossil fuels drove high valuations for renewables from cash-rich investors, globally. Solar and wind were the most invested subsegments among renewables with deal value amounting to US$18.4b across Americas and Europe.

In Europe, renewables investment is expected to accelerate to offset short-term fossil fuel investment, with the European Union's (EU) commitment to achieve net zero by 2050 unchanged. Also, the EU's recently announced REPowerEU agenda focusses on "front-loading" of wind and PV to speed build-out and an extra 80GW of capacity to support more green hydrogen production. While in the US ~70% (60GW) of the new capacity projected to be added in 2022 is tied to renewables, with majority being solar (41.1GW) additions followed by wind (20.5GW).

Companies are undertaking transactions for profit-taking to enhance financial flexibility

In Q1 2022, globally there were around 10 deals involving disposal of regulated transmission and distribution assets amounting to US$2.1b. In one of the interesting deals, YTL Power, a Malaysian power generation company, sold its 33.3% stake in ElectraNet Pty Ltd, an Australian power transmission network services company for US$731m to a group of Australian financial investors. Regarding the transaction, YTL Power commented that the disposal was optimal in light of current attractive valuations of regulated utility assets and would provide financial flexibility to invest in renewables.

Healthy market performance of oil and gas (O&G) companies could drive their continued penetration into clean energy technologies

Energy (O&G) was the best performing sector in 2021, among 11 broad select sector Standard & Poor's Depositary Receipts of S&P 500, with a total return of 53.3%. At the time of writing this, energy (O&G) continued to outperform by being the only sector trading in green so far in 2022. This upward trajectory in stock currency is expected to continue on the back of continued disruption in O&G supply (due to unfortunate ongoing war in Ukraine), driving the energy prices high. This would ultimately increase the purchasing power of these O&G companies, which can be expected to materialize into investments in energy transition.
In Q1, there were six deals where O&G firms invested in renewables, hydrogen and batteries across all regions (Americas, Europe and Asia-Pacific). In one of the recent deals, Royal Dutch Shell agreed to acquire 49% in an Australian wind farm developer, WestWind Energy, which plans to develop 6GW of wind capacity in the next two years, representing its first investment in wind in Australia. In another interesting deal, Baker Hughes acquired a 20% stake in a growth stage company that is developing turquoise hydrogen production technology, for US$62m.

Deal market dynamics are leading to valuation disparities and contentious views on stranded assets

Recently, AGL Energy Ltd (AGL), Australia's largest energy generator, received an unsolicited takeover bid for US$6b from a consortium of Grok Ventures and Brookfield Asset Management. The buyers proposed to shut its nationwide coal plants early and build-out its replacement capacity. In response, AGL rejected the bid citing that the proposal undervalued the company. In another event, Origin Energy proposed to close its 2.8GW Eraring power station in 2025, seven years earlier than previously advised, owing to stressed economics of the power plant due to increasing pressure from clean energy low-cost alternatives, including wind, solar and batteries.

US emerges as the largest bidder with deals amounting to US$23.8

Chart 3: Investment activity globally by country, YTD (US$b)

Investor country

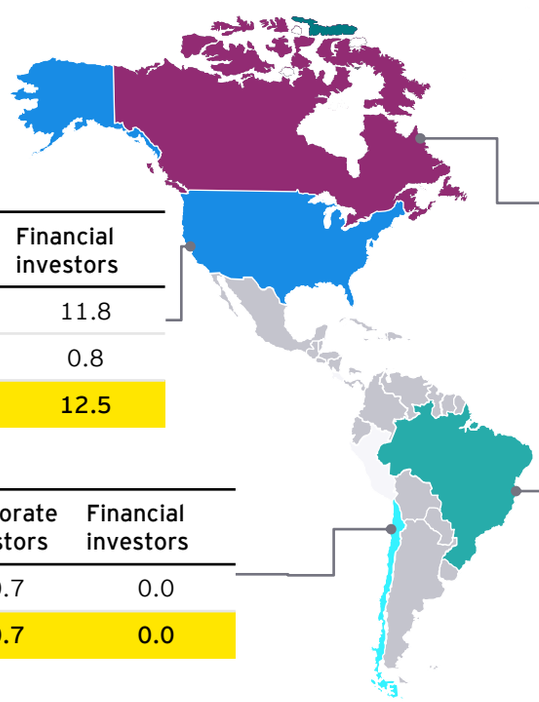
	US	Canada	France	Australia	Italy	China	Brazil	Russia	Switzerland	Japan	Rest of the world	Total receipts
UK	10.5		3.9								0.03	14.5
US	11.8	1.4										13.2
Australia		6.0		0.7								6.7
Canada	0.5											0.5
France			0.01	2.7					0.6			3.3
Italy					1.5							1.5
China						1.2					0.1	1.3
Japan	1.0									0.1		1.1
Brazil							1.0					1.0
Russia								0.9				0.9
Rest of the world		0.7	0.1	0.2	0.7	0.6			0.1	0.6	2.1	5.1
Total receipts	23.8	8.2	4.1	3.6	2.1	1.8	1.0	0.9	0.7	0.7	2.2	49.3

0-5 | 5-10 | 10-20 | 20+

Source: EY analysis with data sourced from Mergermarket.

Note: Numbers may not add to total due to rounding.

Chart 4: Americas investment flow by country and investor, YTD (US$b)



Investor country	Corporate investors	Financial investors
US	0.1	11.8
Canada	0.7	0.8
Total	0.7	12.5

Investor country	Corporate investors	Financial investors
US	0.1	0.5
Total	0.1	0.5

Investor country	Corporate investors	Financial investors
Canada	0.7	0.0
Total	0.7	0.0

Investor country	Corporate investors	Financial investors
Brazil	0.7	0.3
Total	0.7	0.3

Target regions

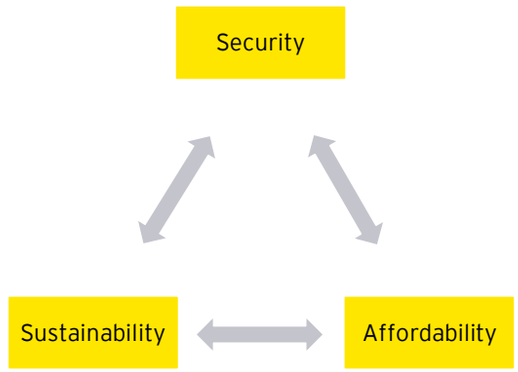
USA Canada Brazil Chile

Note: Numbers may not add to total due to rounding.

Energy security is now becoming the dominant focus in the energy trilemma

Since the start of the war in Ukraine, Europe's fundamental priorities in the energy trilemma are shifting away from sustainability and toward security.

The European energy crisis is driven by many countries having a generation mix that is highly dependent on key fuel imports from Russia. Germany and Italy are the two regions at highest risk, due to their high coal and gas in generation mix and high-import dependency. Overall, Russia provides ~30%–40% of gas supply to Europe and is the largest single supplier.



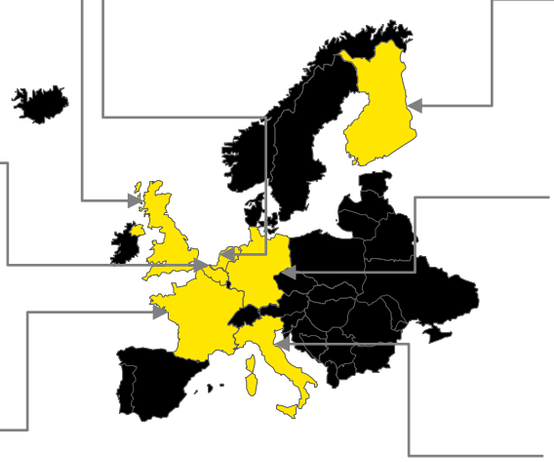
In the past few months, there have been many unprecedented decisions taken by European nations to reduce Europe's dependency on Russian gas imports and to mitigate future supply risks.

UK
- Announced to phase out Russian oil and coal by end of 2022 and Russian LNG gas imports as soon as possible thereafter

Netherlands
- Ramped up building of offshore wind farms, doubling the planned capacity by 2030, to meet climate goals and reduce dependence on Russian gas

Finland
- Constructing new nuclear plants that are expected to meet 14% of power demand by 2025

Belgium
- Reversed its decision to close nuclear power plants
- Increased its offshore wind target to 8GW by 2030



Germany
- Refused to approve the Nord Stream 2 Baltic Sea gas pipeline project (55bcm), from Russia
- Accelerating deployment of two LNG terminals

France
- Planning on building up to 14 nuclear reactors by 2050, with construction potentially beginning in 2028

Italy
- Secured additional supply from Algeria and further plans to look at Azerbaijan, Qatar, Congo, Angola and Mozambique to reduce dependency on Russian gas
- Examining potential to reopen coal units

Furthermore, Russia also has significant market share in the production and export of metals. As such, the supply of raw materials, base metals and components integral to the utility sector may be disrupted. While there are no sanctions on Russian metals to-date, there is a risk of rising battery costs as nickel prices remain high. The ongoing war could lead to metal shortages and a significant increase in prices, which in turn could hit electric vehicle (EV) manufacturers and energy storage companies. New renewable capacity may also be stalled by these disruptions to the metal supply chain.

The energy mix will remain a long-term challenge for Europe, because local energy prices are likely to remain high for many years. While decarbonization is still on the long-term agenda, European governments have a clear focus on ensuring security of supply for national energy independence. Capital investment in infrastructure will be key, with significant capital flows likely to go to fossil fuels such as LNG and coal in the short term, and renewables in the longer term.

Governments must evaluate, **"Who do we trust with our energy dependency?"**

Americas deals summary

US led the region with US$13.2b investments, highest in the past eight quarters

Americas witnessed a total of 33 deals in Q1 2022, with a cumulative deal value of US$15.5b. The deal value was primarily driven by the US, with deal value totaling up to US$13.2b (85% of the total Americas deal value). The dealmaking activity reached in the US was the highest across the past nine quarters. Within these US deals, 85% of the deal value was due to two major multibillion-dollar deals in the gas utility and renewables segment amounting to US$13.15b. Further, 94% of the deals in the US included financial investors.

In the largest multibillion-dollar deal in the Americas, Infrastructure Investments Fund (IIF), a group within JP Morgan agreed to acquire a US-based gas utility for US$7.6b. The deal reflects how utilities continue to be attractive to investors, even at a time when many clean-energy advocates are pressing for states to phase out use of fossil fuels, particularly natural gas.

In contrast to the US, Latin American deal activity was subdued with deal value amounting to US$1.7b, the lowest in the past seven quarters. South American deals were concentrated in Brazil and Chile.

Chart 5: Americas deal value and volume by segment
(Announced asset and corporate-level deals, Q1 2020–Q1 2022)

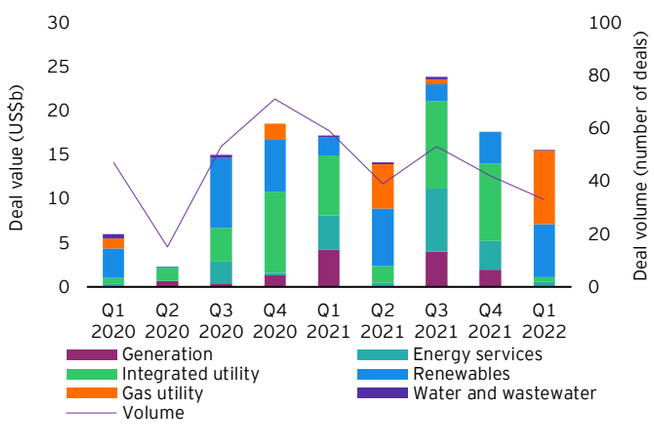
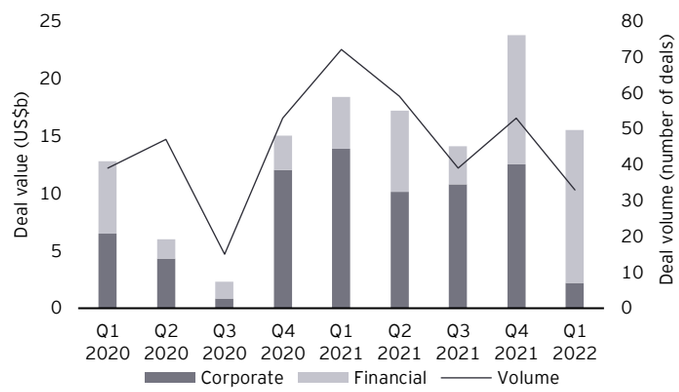


Chart 6: Americas deal value and volume by investor type
(Announced asset and corporate-level deals, Q1 2020–Q1 2022)



Source: EY analysis with data sourced from Mergermarket.

01

Gas local distribution companies (LDCs) highly valued by infrastructure funds

In Q1 2022, South Jersey Industries entered into an agreement to be acquired, in an all-cash deal, by Infrastructure Investments Fund for US$7.6b. The deal was the largest in the Americas. The per-share purchase price of US$36 reflects a 46.3% premium on average 30-day recent trading stock. The deal indicates attractiveness of regulated businesses within investors owing to steady and reliable profits. In another deal, Dominion Energy sold its Hope Gas to Ullico Inc.'s infrastructure fund for US$690m. The transaction's 26.2x P/E and 2.0x rate base multiples screen attractively relative to current sector levels and represent another positive LDC valuation marker.

02

Liquid market for renewable energy deals driven by aggressive private equity firms and infrastructure funds

There were a total of 20 deals in renewables totaling US$6b across the Americas. The US accounted for the maximum deal value of US$4.8b across 10 deals. In the biggest deal, Blackstone invested US$3b in Invenergy Renewables for a minority stake as part of its strategy to invest in energy transition. In another deal, Silicon Ranch, a US-based solar company raised US$775 million in new equity capital from Manulife Investment Management with existing shareholders, including Shell, TD Greystone Infrastructure Fund (Global Master) L.P. and Mountain Group Partners.

Latin America saw the lowest quarterly deal value since Q3 2020 at US$1.7b

03

Financial investors take lead in dealmaking

Financial investors were involved in 17 deals with total value of US$13.3b (85% of total deal value across Americas). These investments were led by JP Morgan and Blackstone Infrastructure Partners (Blackstone), Manulife and Ullico. Among segments, gas LDC assets, renewables and energy services were the three preferred segments of investment respectively in terms of deal value.

04

Canadian deals were driven by energy services

The energy services segment in Canada saw US$524m investments from US-based investors. In the largest deal in the country, Goldman Sachs Asset Management invested US$250m in Hydrostor, an energy storage provider. The investment is among one of the largest commitments by a single investor into a long-duration energy storage company. In another deal, Andion Global, a waste-to-energy solution provider secured US$20m (tranche 1 financing) multi-partner equity financing from Spring Lane Capital, Equitix Infrastructure Investments Limited and Business Development Bank of Canada. As part of the deal, a US$250m project development equity facility will be allocated concurrently. The proceeds are expected to be utilized to expand operations and deployment of waste processing plants.

05

Chile and Brazil dominated the Latin American deals

There were a total of 10 deals in Latin America is Q1 totaling US$1.7b. Out of these deals, nine were in the renewables segment amounting US$1.2b. In the largest deal in Latin America, Innergex Renewable Energy (Innergex) acquired Aela, a 332 MW portfolio of three newly built operating wind assets in Chile for US$686m. The acquisition was in line with Innergex's objective to strengthen its position as a multi-technology renewable operator. Innergex also highlighted Chile as an attractive energy market for investment. In another interesting deal, Brazilian electricity company Energisa Transmissao de acquired the power transmission company Gemini Energy for US$496m, as part of its portfolio diversification strategy away from distribution.

Chart 7: US deal value and volume by segment
(Announced asset and corporate-level deals, Q1 2020–Q1 2022)

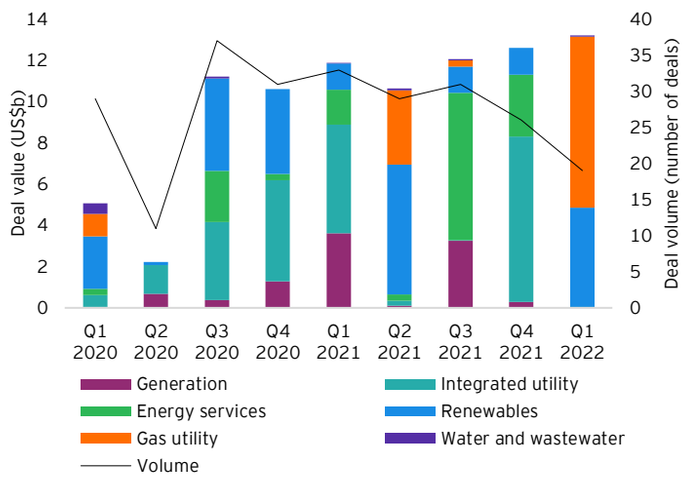


Chart 8: Canada deal value and volume by segment
(Announced asset and corporate-level deals, Q1 2020–Q1 2022)

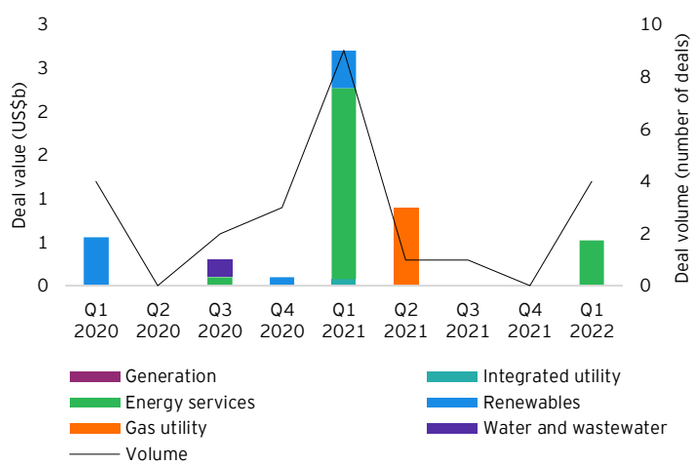
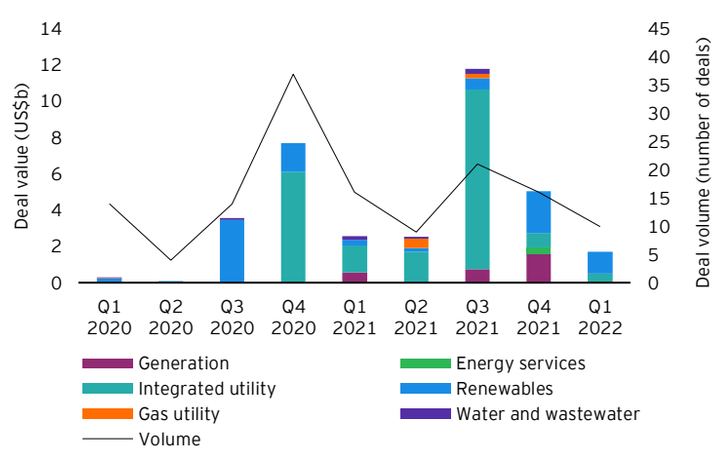


Chart 9: Latin America deal value and volume by segment
(Announced asset and corporate-level deals, Q1 2020–Q1 2022)



Source: EY analysis with data sourced from Mergermarket.

Notable deals in the Americas – Q1 2022 (1/2)

Date announced	Target	Target country/ bidder country	Bidder	Deal value (US$b)	Bidder rationale	Segment
US						
February 24	South Jersey Industries, Inc. (100% stake)	US/US	JPMorgan Chase & Co.; The Infrastructure Investments Fund	7.6	Aligned with IIF's long-term approach to invest in utility and infrastructure assets	Gas utility
January 7	Invenergy Renewables LLC	US/US	Blackstone Infrastructure Partners	3.0	Part of Blackstone's commitment to invest in energy transition	Renewables
January 6	Silicon Ranch Corporation	US/Canada	Royal Dutch Shell Plc; Manulife Financial Corporation; Greystone Managed Investments, Inc.; Manulife Investment Management (Manulife); Mountain Group Capital, LLC	0.78	To capitalize on the expected expansion of renewables (particularly solar) in the US. Also in line with Manulife's strategy to invest in operating renewable assets	Renewables
February 11	Dominion Hope Gas Inc (100% stake)	US/US	Ullico Inc.; Gas Natural Inc.	0.69	Aligns with the bidder's strategy to add large-scale utility in its portfolio	Gas utility
January 26	Urban Grid Solar Projects LLC (100% stake)	US/Canada	Brookfield Renewable Partners L.P.	0.65	To enhance bidder's renewable energy projects pipeline and provides access to key US markets	Renewables
January 19	8minute Solar Energy	US/US	EIG Global Energy Partners	0.40	Aligns with bidder's strategy to invest in renewable energy	Renewables
March 2	H2U Technologies Inc (H2U)	US/Canada	Hess Corporation; VoLo Earth Ventures; Freeflow Ventures; Jericho Energy Ventures Inc	0.01	To accelerate H2U's innovation in hydrogen space	Energy services
February 28	Sofos Harbert (40% stake)	US/Spain	Grenergy Renovables, S.A.	ND	Marks bidder's entry into the US renewable energy market	Renewables
January 4	Triton Utilities Inc	US/US	Ullico Inc.	ND	Expansion of bidder's presence in the regulated utility platform to provide stable long-term cash flows	Water and wastewater
January 7	DB Energy Assets, LLC (100% stake); Beacon Energy Holdings, LLC (100% stake)	US/France	Vauban Infrastructure Partners SCA	ND	Expand bidder's global footprint to the US and demonstrate commitment to sustainability	Energy services
January 27	In-Charge Energy (50% stake)	US/Switzerland	ABB Ltd	ND	Part of bidder's e-mobility growth strategy	Energy services
February 9	Red-Tailed Hawk Photovoltic project (100% stake)	US/Spain	Acciona Energy S.A.	ND	In line with bidder's goal to double its installed capacity in the US by 2023	Renewables
January 14	CertainSolar, Inc.	US/US	The Carlyle Group	ND	Part of bidder's strategic investment in high-growth residential solar industry	Renewables

Source: EY analysis with data sourced from Mergermarket. Note: Numbers may not add to total due to rounding. Note: ND* = Not disclosed.

Notable deals in the Americas – Q1 2022 (2/2)

Date announced	Target	Target country/ bidder country	Bidder	Deal value (US$b)	Bidder rationale	Segment
US						
January 11	BrightNight, LLC	US/US	Global Infrastructure Partners, LLC (GIP)	ND	In line with GIP's strategy to focus on infrastructure projects and companies across power, renewables and energy transition	Energy services
February 2	Constellation Renewables Partners LLC (49% stake)	US/Canada	Axium Infrastructure Inc.	ND	To expand bidder's North American renewable power portfolio	Renewables
South America						
January 20	Contour Global do Brasil Participacoes Ltda (100% stake)	Brazil/Brazil	Patria Investments Limited	0.32	To expand bidder's renewable portfolio	Renewables
February 14	Paracatu and Floresta Photovoltaic Complexes (100% stake)	Brazil/Brazil	Engie Brasil Energia S.A. (Engie)	0.12	In line with Engie's plan to exit from coal and replace it with renewables	Renewables
January 28	50.6 MW San Andres solar farm located in the Atacama Desert in Northern Chile (100% stake)	Chile/Canada	Innergex Renewable Energy Inc.	0.03	Part of bidder's strategy to implement its growth in Chile	Renewables
January 28	Tralka Energias Renovables (18 PMGD photovoltaic projects) (100% stake)	Chile/US	BlackRock, Inc.	ND	Expand presence in Latin America	Renewables
Canada						
January 10	Hydrostor Inc.	Canada/US	Goldman Sachs Asset Management, L.P.	0.25	Opportunity to invest in long duration energy storage	Energy services
February 1	Ekona Power Inc.	Canada/US	Baker Hughes Incorporated; Mitsui & Co., Ltd.; Severstal PAO; ConocoPhillips Company; TransAlta Corporation; BDC Capital; Continental Resources, Inc.; NGIF Cleantech Ventures	0.06	To enhance its broader hydrogen and natural gas decarbonization solutions portfolio	Energy services

Source: EY analysis with data sourced from Mergermarket. Note: Numbers may not add to total due to rounding. Note: ND* = Not disclosed.

Valuation snapshot

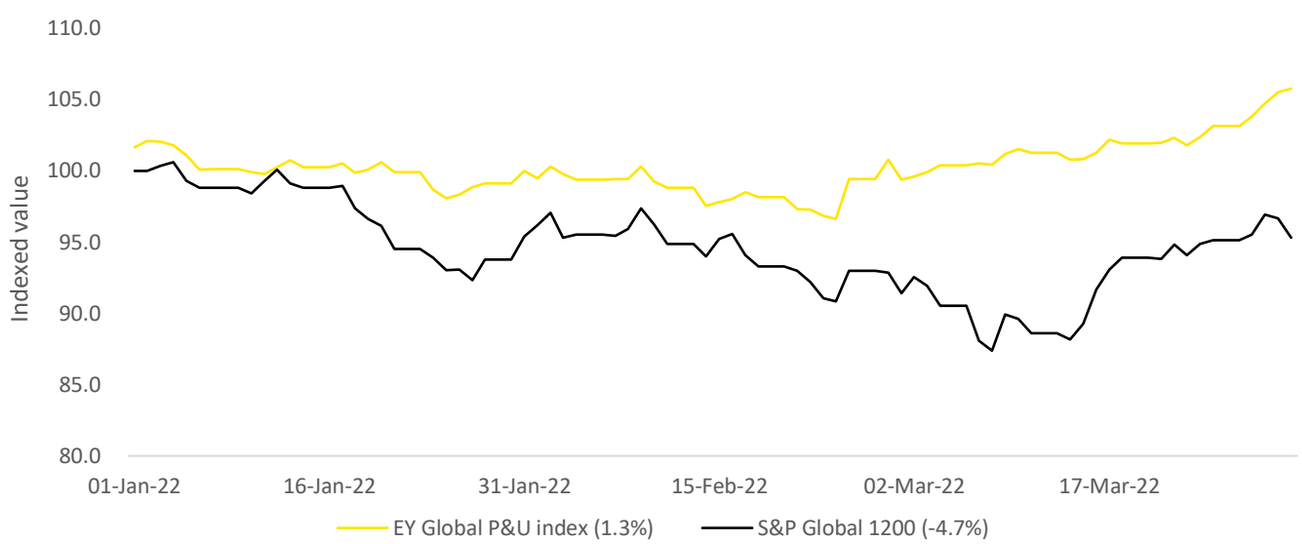
Global valuations and TSR snapshot – Q1 2022

The S&P Global 1200 decreased in value in Q1 compared with the prior quarter, with returns of -4.7% compared with 8.1%. The EY Global P&U index outperformed the S&P Global 1200 with a return of 1.3% for the quarter. The EY Americas P&U index outperformed the broader market with a return of 4.8% for the quarter compared with -4.6% for the S&P 500. Gas utility was the best performing sector in the Americas with a TSR of 13.2% led by South Jersey Industries, Inc. with a TSR of 33.5% and TC Energy Corporation with a TSR of 21.4%.

The EY Europe P&U index underperformed the broader market with a return of -3.4% for the quarter compared with -3.0% for the STOXX Europe 600.

Return over time – from base date

Chart 10: Total shareholder return by region
(from 1 January 2022 to 31 March 2022)

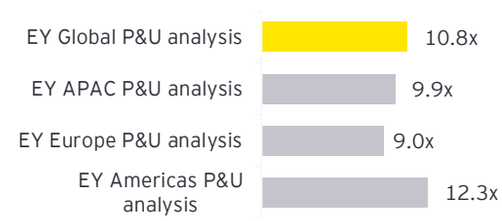


	Americas	Europe	Asia-Pacific
	2021 TSR (%)		
Large market capitalization integrated	4.8	(3.9)	9.9
Medium and small market capitalization integrated	4.0	(8.2)	8.3
Gas utility	13.2	(0.6)	(11.1)
Generation and retail	(7.9)	(7.6)	(7.3)
Renewables	5.9	3.0	15.6
Water and wastewater	(8.1)	(4.0)	(7.6)
Average regional analysis	4.8	(3.4)	0.2

Value of TSR more than the regional sector average

Value of TSR less than the regional sector average

EV/FY+1 EBITDA
(At 31 March 22)



Source: EY analysis with data sourced from Capital IQ.

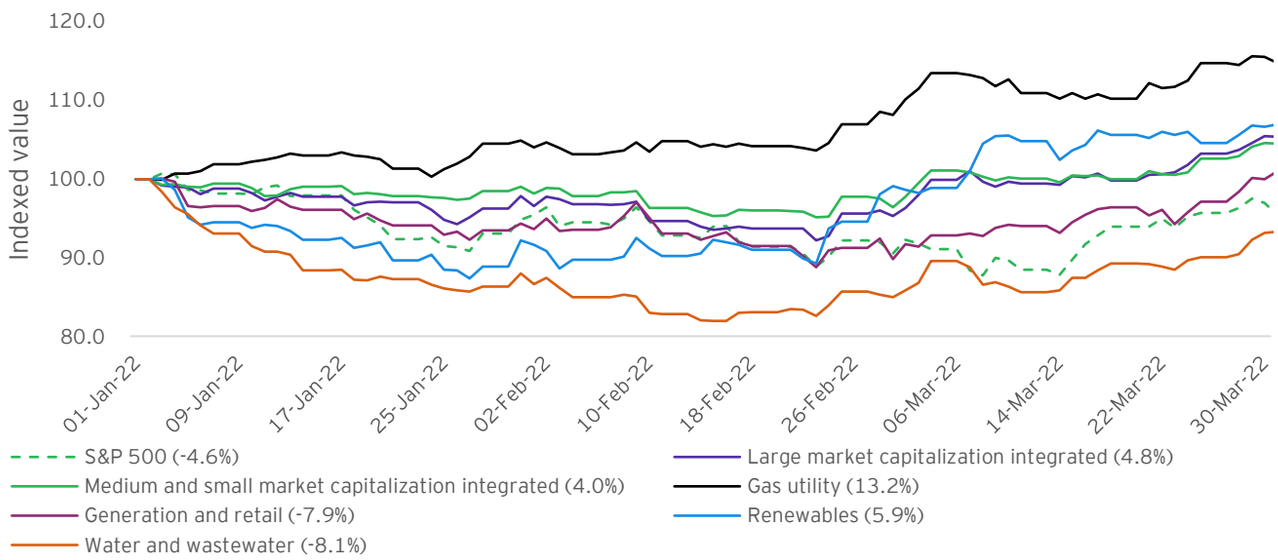
Americas valuations and TSR snapshot – Q1 2022

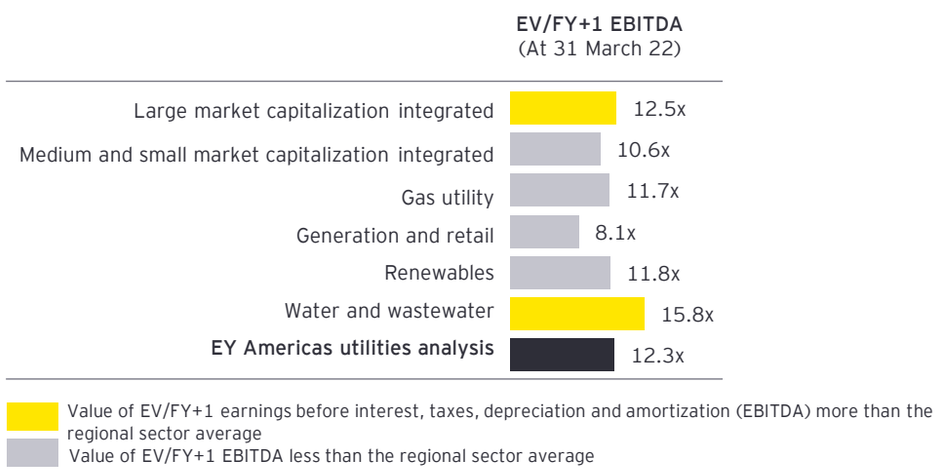
The EY Americas P&U index was the best performing geography in Q1 with a TSR of 4.8% led by South Jersey Industries, Inc. with a TSR of 33.5% and Sempra with a TSR of 28.0%. The EY Americas P&U index had the greatest variance compared with the returns of the local market, retuning a difference of 9.4% compared with 2.9% for the EY APAC P&U index and -0.4% for the EY Europe P&U index.

The best performing stocks for the quarter included South Jersey Industries, Inc. with a TSR of 33.5%, primarily driven by a 46.3% premium as result of its acquisition, and Sempra with a TSR of 28.0%.

Return over time – from base date

Chart 11: Total shareholder return by segment
(from 1 January 2022 to 31 March 2022)





Source: EY analysis with data sourced from Capital IQ.

The utilities in the EY Americas P&U analysis were the highest-valued geography in Q1 with an EV/FY+1 EBITDA of 12.3x led by American States Water Company with an EV/FY+1 EBITDA of 19.4x and American Water Works Company, Inc. with an EV/FY+1 EBITDA of 18.2x. The large market capitalization integrated segment ranked second among segments in the Americas with an EV/FY+1 EBITDA of 12.5x.

4

M&A outlook and investment hotspots

Geopolitics and other economic factors will be forces to reckon with in the deal market

Rising inflation, high interest rates, labor shortage, supply chain disruption, geopolitical tensions and the Washington gridlock pose major challenges going forward.

Portfolio optimization and carve-outs will continue to drive M&A

Companies will opportunistically divest undervalued businesses to enhance their investment opportunities in businesses that are core to their strategic growth pillars and viewed more favorably by shareholders. Utilities will be intentional and seek out ways of redirecting capital toward regulated businesses to de-risk their business portfolios and generate more predictable returns. There will be continuous review for existing portfolios to determine whether a better owner of certain businesses exists for portfolio optimization purposes. Whether such potential transactions serve to offset near-term equity needs or ultimately fund utilities' long-term capital investment plans, we expect utilities will remain disciplined and opportunistic with their capital markets plans.

M&A is expected to become ever more expansive for buyers as public market sentiments toward gas utilities continue to improve

Several recent gas utility deals, including, but not limited to, South Jersey Industries, Hope Gas, and CenterPoint Energy's gas LDCs in Oklahoma and Arkansas have reaped attractive deal premiums. Given current trading multiples and a more favorable public market's sentiment toward gas utilities, it will be more expensive for financial sponsors to continue their shopping spree. In the context of lofty valuations, multi-utilities with gas LDCs may increasingly be forced to consider whether LDCs are still core to their business while evaluating monetization strategies. While most financial sponsors continue to prioritize electric transmission and distribution, water businesses and renewable energy over gas utility investments, some investors have started to take a contrarian view and see more longevity in the gas utility subsector particularly in certain regions.

Economies of scale to drive down overall cost of service during the inflationary period has the potential to drive transactions

The ongoing war in Ukraine is driving and sustaining a high commodity price environment; high inflation and interest rates; and supply chain disruption issues broadly and in the energy sector, including in renewables. In the face of these challenges, affordability of utility rates will continue to be a key focus area for countries and could drive transactions. Specifically, in Europe, the talks about energy rationing could spark up discussions around energy security and affordability and drive domestic deals. During periods of macroeconomic cycle turning defensive, utilities have benefitted from strong total shareholder returns and valuation, which may be a catalyst for dealmaking opportunities for achieving economies of scale in operations and bigger balance sheets to drive investments in the structural energy transition while at the same time balancing affordability of utility rates.

Regulatory uncertainties will be the most significant challenge dealmakers face

Regulatory M&A approvals are evolving, and precedents do not guarantee outcomes. Public awareness, scrutiny and engagement on complex issues that include consumer data and privacy; national interest and security; job creation; public perception; and environmental, social and governance profile are expected to increase even further in the coming year.

In December 2020, Avangrid announced plans to acquire PNM Resources for US$8b, but in December 2021, New Mexico utility regulators voted to reject the proposal, saying that the deal's risks outweighed its promised benefits to state ratepayers. The companies have again filed numerous arguments with the court in April 2022, in pursuit of having a fair deal.

Dealmakers must learn to navigate the increasingly complex regulatory environment to achieve success. Demonstrating a comprehensive understanding of the local norms, risks, regulatory environment as well as the interests of all stakeholders is expected to be increasingly taxing in anticipation of limited bandwidth at the Public Utility Commission overwhelmed with rate case filings and broader policies initiatives.

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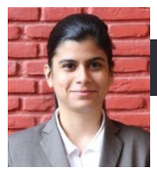

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