
M&A activity in power and utility (P&U) industry



Impact of global events on P&U industry

The M&A deal landscape was significantly affected due to many factors, including increased inflation and interest rates, geopolitical turmoil, and volatile commodity prices. These uncertainties led to a decrease of 57% in aggregate M&A deal value in the P&U sector, from USD 221 billion in H1'2022 to USD 96 billion in H1'2023.

Geopolitical factors

According to International Energy Agency, electricity consumption declined by 3.5% y-o-y in the European Union in 2022, due to high-energy prices influenced by Russia's restrictions on the sale of fossil fuels. Additionally, the average wholesale price for electricity stood at USD 91 / MWh in the US in H2 2022, which is ~65% higher than the H2 2021 price, primarily, due to high gas prices. To mitigate this, the US is increasing investments in renewable & clean technologies by providing incentives under Inflation Reduction Act of 2022.

Decentralization

The P&U industry is transitioning from a centralized power generation and distribution model to a more distributed and localized approach. It involves utilizing renewable energy sources and establishing localized microgrids to allow consumers to generate their electricity. This is in line with the increasing demand for renewable energy and the need for resilient power grid. An example of this can be seen in Glasgow, Scotland, where there has been a notable increase in local energy generation from generators in and around the city.

Digitization

Due to high demand, distributors and transmission system operators are investing in new smart grids and modernizing aging infrastructure. According to IEA, governments have allocated ~USD 20 billion directly for transmission and distribution system spending since the beginning of the pandemic until 2023. To achieve net-zero emissions by 2050, investment in smart grids requires a significant increase. It is anticipated that this investment will need to surpass USD 600 billion by 2030, more than doubling the current levels.

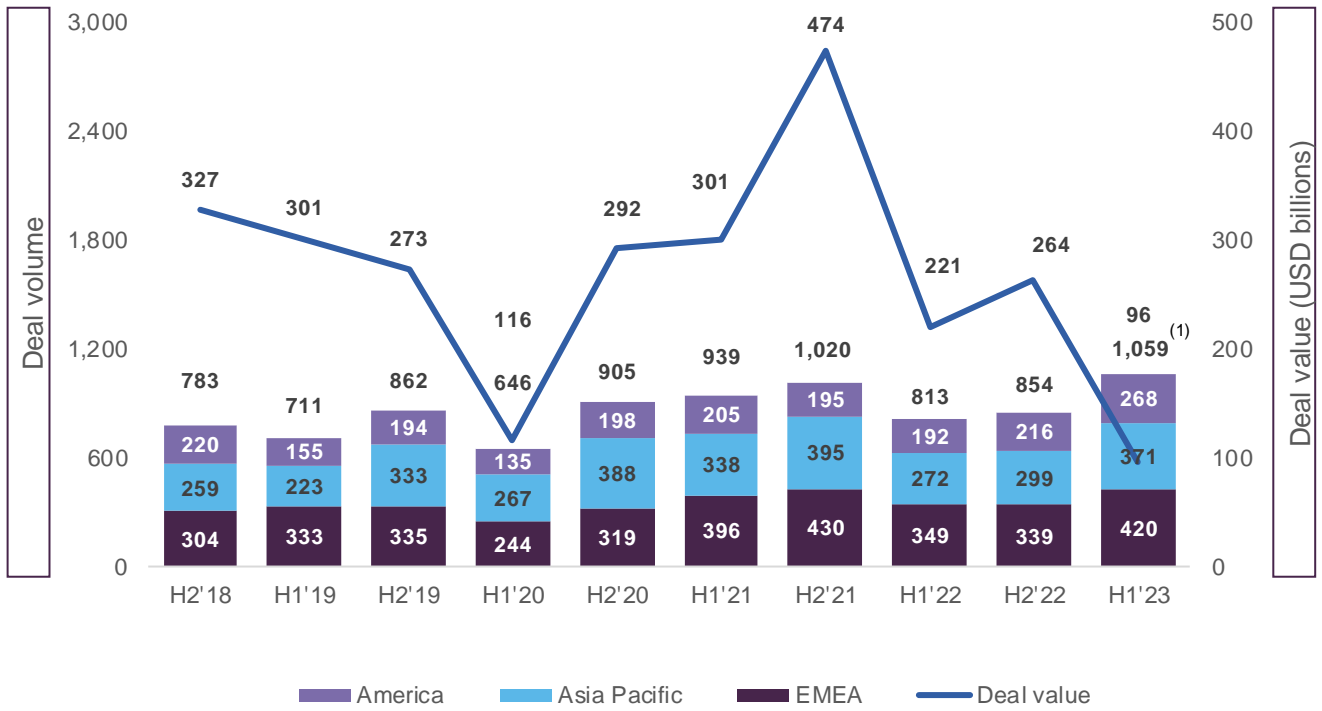
Supply chain disruptions

The renewable energy sector will likely face supply chain disruptions due to increasing raw material costs, specifically to manufacture solar panels. Raw material costs increased by ~20% in 2022. This situation is expected to slow the pace of M&A in the industry. The challenges are projected to continue in 2023, due to shortages of battery and critical mineral suppliers and concerns relating to unethical labor practices.

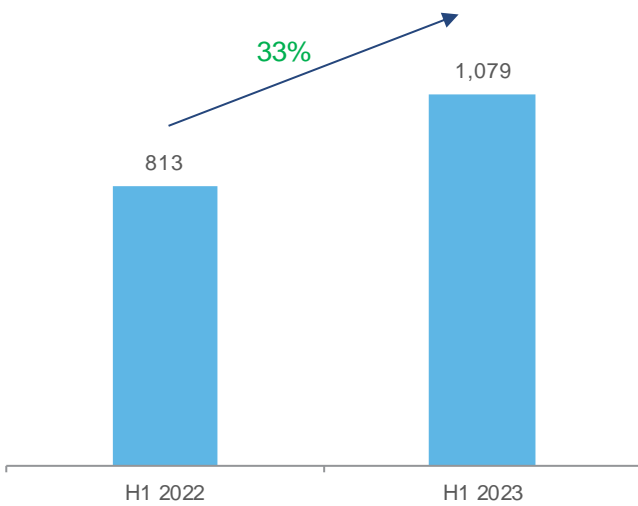
Source: Press releases

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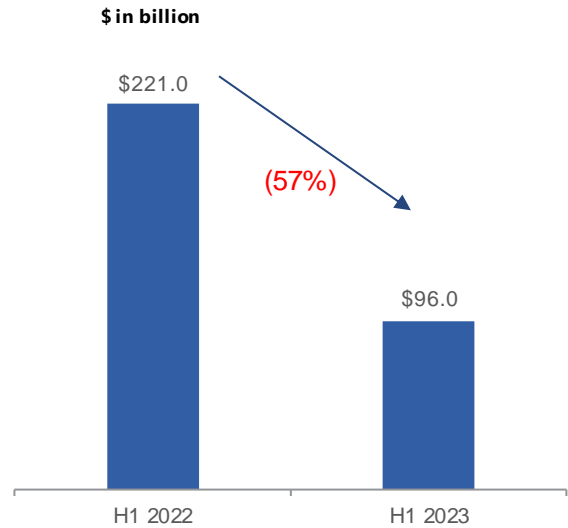
M&A Transactions in H1'2023 drop below pandemic-era levels



Y-o-Y Change in Global Deal Volume



Y-o-Y Change in Global Deal Value



Source: PwC, Power technologies and Global data

(1) Region wise details are not available in H1'2023, hence extrapolated from H2'2022 numbers

Top announced M&A by transaction value (YTD 2023)

| Announcement date | Target | Target's advisor | Transaction value (USD billion) | Acquirer | Acquirer's advisor |
|-------------------|--------------------------|--|---------------------------------|--|---|
| 12-Jun-23 | Iberdrola Mexico | JP Morgan | 6.0 | Mexico Infrastructure Partners | Barclays |
| 12-Jun-23 | Duke Energy Renewables | NA | 1.1 | Brookfield Renewable | Scotiabank, BMO Capital Markets, TD Securities Inc., CIBC Capital Markets |
| 16-May-23 | ASR Wind | Banco Santander | 0.7 | Naturgy Energy | NA |
| 26-Apr-23 | Total Energies EP Canada | NA | 4.5 | Suncor Energy | JP Morgan Securities Canada, Blake Cassels, Graydon, and Paul, Weiss, Rifkind |
| 2-Feb-23 | FirstEnergy Transmission | JP Morgan Securities, Citigroup, Moelis & Company, and Jones Day | 3.5 | Brookfield Asset Management (Infrastructure) | Skadden, Arps, Slate, and Meagher & Flom |
| 6-Mar-23 | Energy Harbor | Goldman Sachs, RBC Capital Markets, Dechert, Morgan | 3.0 | Vistra Corp. | Citi, Latham & Watkins, and Balch & Bingham |
| 22-Mar-23 | Parkwind NV | UBS, Linklaters | 1.7 | JERA | Morgan Stanley, Mitsubishi UFJ |

Source: Company press releases & Global data

Key trends and drivers of P&U industry

The M&A in the P&U industry is anticipated to be impacted by various factors, including the energy transition, technological advancements, investor interests, and regulatory policies. Some key trends include the following:



ESG and sustainable investments

According to PwC's projections, asset managers worldwide will increase their ESG-related AuM to USD 33.9 trillion by 2026. ESG-influenced investment and M&A has been gaining prominence, i.e., the big players are acquiring new clean energy players. Key M&A include Ørsted's acquisition of Lincoln Clean Energy, Iberdrola's acquisition of UIL Holding, and E.ON's acquisition of Innogy.



Mobility electrification

The global electric mobility market will likely post a CAGR of 14.6% to reach USD 325.64 billion by 2030, primarily driven by the increasing adoption of EVs, which will, in turn, increase demand for charging infrastructure and trigger M&A activities in the power sector. Notable M&A examples include Shell's acquisition of NewMotion, Enel's acquisition of eMotorWerks and Total's acquisition of Saft.



Repositioning of portfolio toward energy transition

Businesses are using M&A as a strategy to accelerate their portfolio transformations, by investing in the energy transition while simultaneously divesting high-carbon assets. M&A activities are influenced by the sensitivity of big players in the industry toward carbon neutrality. A few key examples are Total's acquisition of SunPower, Engie's acquisition of Renvico, and Brookfield's acquisition of TerraForm.



Technology advancements

The sector is undergoing a technological transformation due to the adoption of AI, IoT, and blockchain. These technologies will support companies with predictive maintenance, demand forecasting and grid optimization. To leverage the benefits, P&U companies seek opportunities with players from the sector. For instance, American Electric Power acquired Enlighted, an IoT solutions provider.



Smart meters and smart grids


Globally, businesses are prioritizing the development and integration of smart meters and smart grids. Global System for Mobile Communications Association estimates that North America, will host 1.4 billion smart buildings. The M&A space is experiencing the impact of this shift. For instance, in January 2023, Badger Meter announced acquisition of Syrinix, a provider of intelligent water monitoring solutions.

Source: Company press releases

Effects of rate base on M&A activities in P&U industry


As per the data tracked by Regulatory Research Associates, investor-owned utilities in the US asked for rate hikes totaling USD 16.89 billion in 2022, up by 14% from a record-breaking 2021. The rate base has a notable effect on M&A in the P&U industry. A few examples rate base's influence on M&A activity are as follows:

A higher rate base indicates a large asset base, which can increase financial stability. M&A often aim to achieve operational synergies and cost savings. Combining rate bases can lead to economies of scale and improved efficiency. For example, in 2020, NextEra Energy acquired Gulf Power for its substantial rate base and stable cash flows. Similarly, in 2012, Duke Energy and Progress Energy merged to create one of the largest electric utility companies in the US. The consolidated rate bases helped them achieve operational efficiencies.



Increased financial stability and synergy potential


Source: Company press releases



Regulatory considerations

M&A transactions in the P&U industry often require regulatory approvals, and regulators consider the rate base during the review process. For instance, Exelon Corporation's acquisition of Pepco Holdings faced regulatory scrutiny in 2016, due to concerns relating to the impact on the rate base and customer rates. Regulators evaluated the benefits and risks of the transaction, considering how the rate base of the combined entity would affect customers and the overall market.

Acquiring a company with a significant rate base can provide growth opportunities for the acquiring company. By expanding their rate base, utility companies can potentially increase their customer base and revenue. In 2019, Avangrid, a subsidiary of Iberdrola, acquired PNM Resources, which brought together their respective rate bases and created a larger entity with enhanced growth prospects.



Growth opportunities

The rate base plays a crucial role in evaluating the financial stability, regulatory considerations, growth opportunities, and potential synergies in M&A transactions in the P&U industry.

Source: Company press releases

Outlook for P&U industry

The power generation industry is experiencing a surge in M&A as renewables are all set to dominate the market due to increased sensitivity toward net-zero emissions. M&A activity in the transmission sector is also inclining towards resilient smart grids, decarbonization, and digitalization. Further, the distribution industry is witnessing significant growth due to advancements in data centers, smart grids, and privatization, which has boosted M&A activity.



Generation

Consolidation amid transformation from non-renewable to renewable energy

To adhere to stringent environmental rules, the smaller competitive businesses aim to combine with existing giants, leading to an M&A boom. Since the power generation industry accounts for 40% of CO2 emissions, the countries globally are switching to renewable energy. The electricity sector, the biggest CO2 emitter, aims to achieve net-zero emissions by 2040. Nuclear power and renewable energy sources will collectively supply around 90% of the additional worldwide demand by 2025.



Transmission

Transmission through grid resilience, decarbonization, and digitalization

After Russia's invasion of Ukraine, countries have shown integration with renewable energy networks and grid expansion, which will have positive effects on the growth of this industry globally. The EU is also focusing on the following to enforce renewable integrations:

- Interconnection target with neighboring regions from 10% of import capacity over installed generation capacity to 15% by 2030
- Adding 128 GW of new interconnector capacity by 2040; HV grid capacity in China will double by 2050, and more than 35% of grid assets in the US will be replaced by 2040.



Distribution

Datacenter advancements, smart grids, and privatization for efficient power distribution

The power distribution unit market is expected to post a CAGR of 4.6% to reach USD 4 billion during 2022–32. Companies are actively indulging in M&A and investing in the following:

1. Advancing their data centers for a better electricity supply
2. Using ~70% of above investment will be used for expanding, strengthening, and digitalizing networks of distribution grids
3. Adopting the privatization model in the distribution sector, such as franchise models and public-private partnerships, and introducing competitive bidding for distribution licenses in some areas

Conclusion

The P&U industry has experienced a notable decline in M&A activity recently primarily due to various factors such as inflation, high-interest rates, geopolitical uncertainties, and volatile commodity prices. Despite this downturn, the M&A landscape is expected to regain momentum in the near to medium term. Factors driving this anticipated resurgence may include the availability of abundant capital, a focus on energy transition, growing interest in supply chain security, and increasing awareness of potential value opportunities within the current macroeconomic climate.

Source: Company press releases

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