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Utilities' Perfect Storm Bodes Well for Smart Grid

A perfect storm is brewing for utility companies: Assets and infrastructure are outdated, long-term demand is outstripping supply, environmental regulations are becoming increasingly stringent and legacy information technologies systems offer little help.

Utilities are turning to smart grid technologies to help solve these problems. Traditional automated meter reading (AMR) and advanced metering infrastructure (AMI) vendors are working to meet this demand, expanding their product and service portfolios through acquisition and internal development. Yet traditional vendors are facing more competition from new entrants—big and small—eager to tap this burgeoning industry.

While the industry has been growing rapidly for more than a decade, the U.S. government's \$4.5 billion investment in smart grid technology will accelerate adoption.

"Once the government acts on this stimulus objective, expect utilities to start massive deployments," said Howard A. Scott of Cognyst Advisors, LLC during a hosted institutional investor call with Stephens in February.

During the next four to five years,

vendors will compete for U.S. smart grid projects, likely culminating with significant saturation among large U.S. utilities. As a result, forward-thinking smart grid players are considering international opportunities, as well as gas and water applications.

Consolidation and acquisitions quickly follow rapid upticks in demand, adoption of new technologies and an emergence of new competitors. Expect to see acquisitions ramp up in the next 12 to 24 months as equity and credit markets stabilize and as vendors seek to build scale and depth to capture North American and worldwide market share.

NEW MARKET ENTRANTS

During the past decade, AMR has evolved into AMI, which has further evolved into the smart grid. As evidenced at the annual industry conferences, companies and technologies are using the smart grid moniker for their services and products. While traditional AMR and AMI players dominate market share in the sector, other smart grid participants are starting to capture industry attention:

- Accenture recently hired Sharon

Allan from Elster Integrated Solutions (EIS) to lead its smart grid initiatives. Accenture has more than 30 projects across 15 countries and recently launched an Intelligent City Network, a collection of utilities and cities that share progress, challenges and solutions.

- In April, Cisco Systems partnered with GE and Silver Spring Networks on the Energy Smart Miami project with Florida Power & Light. The entrance of Cisco into the smart grid arena with partners such as GE and the fast-growing, multiple project-winning Silver Spring has drawn industry observers' attention.
- In March, AT&T struck a deal with smart grid company SmartSynch to act as a communication platform among individual residential meters.
- In February, Google introduced its PowerMeter program that will allow consumers to view energy consumption courtesy of smart meters in near real-time via iGoogle.
- As the largest provider of information technologies solutions for the U.S. government,

Lockheed Martin has become more active in the smart grid space, most recently investing in smart grid research and development alongside Penn State University.

M&A AND JV

To prepare for utilities' aggressive smart grid deployments, smart grid vendors might want to bolster their technology portfolios via joint ventures (JV) or mergers and acquisitions (M&A). Transactions likely fall into one of four categories:

1. Traditional AMR and AMI players will make bolt-on acquisitions, seeking opportunities to build out their subsectors of expertise and consolidate the industry.

For example, Trilliant Inc. announced in May the acquisition of Santa Clara, Calif.-based SkyPilot Networks Inc., a provider of long-range wireless mesh broadband equipment. Trilliant expects its acquisition will open possibilities for advanced networking applications. In November 2008, SmartSynch acquired Applied Mesh Technologies. SmartSynch expects that AppMesh's product suite will enable the company to extend service to customers on multiple levels, including distribution automation, supervisory control and data acquisition (SCADA), generator and load control and electric distribution, steam and plug-in hybrid

electric vehicle monitoring. In prior years, acquisitions also proved to be critical to the growth and strategic positioning of market leaders including Itron (Actaris), ESCO Technologies (Hexagram), Landis+Gyr (Cellnet) and Sensus (AMDS). Following such acquisitions, new business wins have helped these vendors remain at the forefront of the industry, solidifying their presence in front of utilities. Expect smaller, up-and-coming vendors to experience similar rewards from their strategic additions and partnerships.

2. Traditional smart grid vendors will acquire or partner with companies that broaden their capabilities.

In late 2008 and early 2009, Silver Spring Networks announced partnership deals with ABB and S&C Electric to create a unified smart grid network supporting distribution automation, SCADA and AMI. In January 2008, BPL Global acquired Serveron, thereby expanding BPL Global's Power SG software platform reach from the customer premises to the substation. Also in January 2008, Comverge partnered with Eaton to bring demand response and managed energy service offerings to Eaton's customers. And in late 2007, ESCO bought Doble Engineering. Already an AMI leader, ESCO expanded its product and service offerings for electric utilities worldwide

via Doble, which provides diagnostic test solutions for the electric power industry. These acquisitions and partnerships have not been in basic AMI add-ons, but they have added value to participating companies and continue to re-define the smart grid.

3. Large transmission and distribution vendors might acquire AMR and AMI companies to build their positions and gain footholds in the smart grid industry.

While such transactions have yet to ramp up, many vendors are partnering with technology companies that provide transparent pathways. GE, already in the metering business, has made numerous acquisitions including 2008 purchases of Irish smart grid firm Kelman Ltd. and MapFrame, a provider of mobile mapping and field automation technologies for utilities' employees. In addition, GE announced a global original equipment manufacturer agreement with Industrial Defender, a cybersecurity technology integrated with smart grid automation technologies. AREVA's technologies focus on electricity transmission and distribution. It designs, manufactures and supplies equipment, systems and services for all stages in the transfer of electricity, from generators to large end-users. Recently, AREVA's transmission and distribution division extended its three-year

collaboration with Microsoft to include the development of smart grid management solutions. And Siemens has a stake in SmartSynch and eMeter. Will world-leading companies like those mentioned consolidate the AMI and smart grid industry? Expect long-term strategic positioning to angle toward the smart grid.

4. Companies outside power, energy and resource technology industries are concentrating efforts (through M&As or partnerships) to get in on the action before global utilities widely accept smart

grid technology. Companies such as Cisco, AT&T and Google have entered the smart grid arena. We expect more, although it is too early to tell if such companies will move forward in the partnership format or stake out a more formal position in the smart grid arena via acquisition.

With billions of dollars of federal stimulus aimed at smart grid technologies, there is room for cooperation and competition. Industry players are positioning themselves for a profitable smart grid build-out in the years ahead. Acquisitions can

change the fundamental dynamics of an AMI and AMR business or help new entrants gain industry footholds. By redefining the breadth and scope of the services, companies can reposition themselves as smart grid players better able to meet the demands of utilities for years. ●

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