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M&A Team of AEG Affiliated Energy Group Closes 3 M&A Deals in Past 9 Months; Expects More in Coming Quarters

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AEG Affiliated Energy Group has closed three mergers and acquisition deals specifically in the retail energy space in the past nine months, and expects more deals to close in the next two quarters.

As first reported by Matters, the team of AEG Affiliated Energy Group recently served as Frontier Utilities' sole investment bankers in its sale to a group of independent Texas-based investors led by Quintana Infrastructure & Development LLC and industry veteran Jay D. Hellums.

As previously reported, AEG also represented Kinetic Energy in its sale, and was buy-side advisor to Cirro Energy (a unit of Dominion Retail) in its purchase of Simple Power. In addition, AEG's team recently negotiated two successful financing and credit facility deals in the retail energy space, both of which remain confidential.

"AEG's M&A Team has an active pipeline of M&A deals in progress and anticipates more M&A deals being closed within the next two quarters," said Chad Price, Co-Chair of AEG Affiliated Energy Group's M&A Practice.

Price elaborated that AEG continues to work on "multiple" M&A retail electricity and gas transactions, most of which consist of parties either in the Northeastern and Midwestern markets, or parties in ERCOT, but Price could not disclose details at this time.

AEG
Affiliated Energy Group
Mergers and Acquisitions Division
Specializing in Retail Energy Markets.

With interest rates near historical lows and a significant number of investors and established utilities with strong balance sheets and liquidity, Rob Potosky, Esq., Co-Chair of AEG Affiliated Energy Group's M&A Practice, said that AEG continues to see strong interest in retail energy suppliers with, "strong unlevered free cash flow and LTM EBITDA, significant synergy-potential, scalability, proprietary assets such as in-house billing systems or efficient distribution systems, proven marketing channels/ strategies, experienced wholesale supply teams, sticky hard-to-duplicate customer portfolios, strength of brand-name, experienced management teams, among other valuable assets."

Discussing some additional factors which affect the valuation of retail providers, Potosky noted, "some of the smaller REPs and ESCOs may fail to realize the extent to which a poorly negotiated long term lockbox supply/credit facility can directly and indirectly impact their company's valuations until it's too late."

Potosky confirmed that ERCOT has seen fewer distressed retail providers, and accompanying sales, than anticipated by some market observers after the extreme weather of the summer, which many predicted would strain retail providers' finances.

None of AEG's recent transactions were distress deals.

Since the February 2011 rolling outages, there has only been a single POLR event, and less than a handful of truly distressed transactions -- certainly not anywhere close to the fire-sales and defaults seen after the 2008 congestion, or 2005-06 natural gas price spike.

Potosky reiterated, as AEG previously told Matters,, that the lack of any large scale market exits after this summer can be attributed to, among other reasons, the presence of lockbox and financing agreements which retail suppliers had in place with creditworthy suppliers, "who tended to forgive breaches of financial covenants and late payments in exchange for renewed or extended lockbox terms and/or higher administrative and sleeve fees, rather than foreclosing on such parties' businesses."

In light of this past summer, and minimal reserve margins that may produce more scarcity pricing this summer, Price reported that many retail providers have become more conservative, and more of the smaller retailers, "seem willing to pay the premiums associated with super peak products, versus buying straight block (peak, off-peak, and the round-the-clock) products."

While demand has also increased for weather-adjusted profiles and insurance-type products, Price said that, "some retail suppliers continue to view such products as having over-inflated premiums, limited liquidity, and high bid ask spreads."

"Tempering appetite for such products, AEG also believes there is significant counterparty credit risk with at least one of the very few counterparties offering weather adjusted profiles in certain sub-markets, thus making such long term products more risky and less useful than may be apparent," Price added.

Price reported that AEG has also seen some retail providers preferring to err on the side of being long versus short, through the purchases of block products above their forecasted requirements for significant portions of their aggregate load profile during the coming summer months, as an alternative to buying shaped load products.

Asked about new minimum capitalization requirements that will soon be in place in ERCOT, Potosky said that some retail providers may seek to improve overall capitalization through capital contributions, retaining more earnings, leaning on lockbox providers to reduce working capital requirements and/or improve cash flows, or possibly by indirectly procuring credit and reducing working capital needs through the use or retention of a QSE that is long and that can net out short positions cheaply.

In consummating and closing the business combination with Frontier Utilities, AEG's M&A team members, which are licensed investment bankers, acted in their capacity as licensed securities agents of Burch & Company, Inc. ("Burch"), Member FINRA (www.finra.org) & SiPC (www.sipc.org), and all services that are required to be performed by a registered broker-dealer were and are offered through Burch.