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The Water Industry 2021

Environmental Business International Inc.

WATER INDUSTRY HITS \$200 BILLION

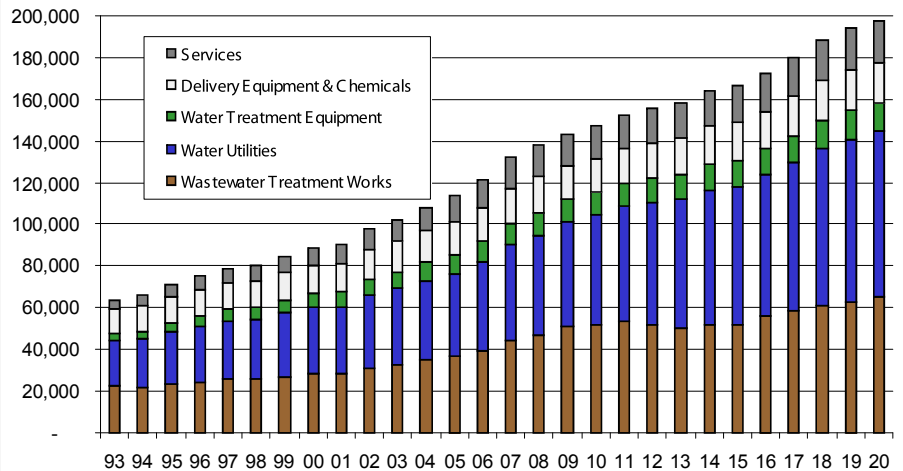
The history of humankind changed with the use of fire as long as a million years ago, but most historians accept the argument that the dawn of civilization came with the development the first water infrastructure systems 7,000 years ago. While the Romans are generally glorified for their advances in water and wastewater infrastructure, many cultures developed systems to store and convey drinking water and manage waste.

It is only in recent history, however, that the water industry has truly taken shape as a definable commercial enterprise, emerging from a public service to distinct business segments capable of supporting investment and return. The water industry is still a work in progress, however, as public and private interests continue to conflict and overlap in a number of ways, including public access, profit motive, environmental concerns and social equity.

Over the last 30 years of analysis, Environmental Business Journal® has seen an increasing involvement of private interests, and the emergence of global investment propositions in water utilities, water rights, water equipment, treatment technology, and more recently water and wastewater services as attractive segments offering stable recurring revenue streams and capacity for sustained growth.

The U.S. water industry endured the year of COVID-19 better than many industries, posting growth of 1.5% to a total of \$199.5 billion in revenues generated in 2020, according to an analysis by Environmental Business International and published in this edition of Environmental Business Journal®. As has been the case for much of the last 30 years, the overall growth rate was bolstered by the growth of revenues collected by 160,000 water and wastewater utilities in both the private

The U.S. Water Industry, 1993-2020 (\$mil)



Source: Environmental Business International, Inc. Annual research on the water industry by EBI and EBJ in surveys, interviews and compilations of secondary data and company data. See segment information on p.2.

Inside EBJ: The Water Industry 2021

The U.S. Water Industry faces a predictable future of consistent growth, demand, increasing rates and a very likely boost in federal funds for upgrades, but an uncertain future of aging infrastructure, supply imbalances, and threats from climate change. Surveys and data sets curated by EBJ present a picture of a \$200-billion industry rooted in its infrastructure and business segments, but fueled by increasing flows of investment capital and waves of technology innovation..... 1-9

Water Rates Increase; Sources and Uses of Water; Water Use by State & Sector; Lessons from California's Water Funding; O&M Industry Overview..... 10-19

M&A Headlines: Axius Water a Collaboration of KKR and XPV; Solenis Acquired by Platinum Equity; Veolia-Suez Merger; Essential Utilities Passes \$1 Billion..... 20

Cadmus Expands its Strategic & Technical Focus on Water; Remains the Largest Primary Contractor For EPA's Ground Water And Drinking Water Programs 24

CDM Smith's Optimism for the Water Industry Fueled by \$48 Billion in New Funding, and Infrastructure Needs in Efficiency, Resiliency and Sustainability 30

Inframark Adds 14 Private Public Partnerships; Grows to 1,500 People and Inks a New Partner In New Mountain Capital to Up Stakes in the O&M Market..... 35

GAI Consultants Advances Green Infrastructure in Pittsburgh and Florida..... 39

KETOS Leads Water Automation with Integrated Solutions; Raises \$31 Million in Venture Capital and Surpasses 13 Million Data Points 43

Investment Bank Alarian Sees Opportunity in a Water Industry That is Fragmented, Under-Capitalized and in Need of Technology Innovation 46

Ecolab Says Data & Digital Solutions are Key to Water & Climate Change..... 49

INVESTMENT BANK ALARIAN SEES OPPORTUNITY IN A WATER INDUSTRY THAT IS FRAGMENTED, UNDER-CAPITALIZED AND IN NEED OF TECHNOLOGY INNOVATION

Alarian Associates, Inc. is an independent investment banking firm with deep understanding of industrial and environmental services, waste management, telecommunication, construction and energy infrastructure industries, as well as the engineering firms and labor services that support them. The Company is located in New York and provides its services to lower middle market companies, both buyers and sellers, as well as to private equity companies that target key sectors of the US economy primarily, industrial, infrastructure and environmental.

Pauli Overdorff, President and founder. With over 30 years of experience, Ms. Overdorff has significant expertise in the environmental services, waste management, telecommunications, construction and staffing industries. She was the majority shareholder of First Response Environmental Group, Inc. and served as Chairman of the Board prior to the Company's sale to Tradebe USA.

Before founding Alarian, Ms. Overdorff was Executive Vice President of TMP Worldwide and managed the integration of 17 IT staffing and professional services acquisitions that the company made. Prior to TMP, Ms. Overdorff enjoyed 5 years at Spherion capping her tenure as Executive Vice President where she held operational responsibilities for more than \$200 million in North American consulting services. Previously, Pauli has also held senior positions at AGS Computers and Bear Stearns.

EBJ: How would you describe the financial performance of the water sector? What are the major market trends?

Overdorff: The Water Utility Industry is made up of domestic companies, mostly local and regional, responsible for the safe and timely distribution of water and other related services, such as wastewater treatment. Demand from the industrial, agricultural and residential markets is expanding and the supply of potable water is shrinking. However, significant earnings and share-price gains are not a hallmark of financial performance. The industry is subject to regulation, which can raise service costs, while limiting rates and return on investment. Additionally, the sector is mature and capital intensive. Water utility stocks, of which there are 53, are not growth issues, but they do usually offer solid yields and regular dividend increases.

Heavy infrastructure outlays have led to highly levered balance sheets, and the companies have had to carefully manage significant operating costs and interest expense to maintain attractive dividend payout ratios. Water utility equities often

gain popularity when economic times are stressed and the broader stock market is in a downturn. Operations are seasonal, with demand highest during the summer months. Periods of excessively dry or wet weather can cause near-term share-price volatility, but such swings are generally not dramatic.

The nation's water system has suffered from underfunding. Many systems are over a hundred years old and require substantial upgrades, if not complete reconstruction. The EPA estimates that over the next couple of decades hundreds of millions of dollars will need to be invested to bring our water systems up to standard. Good working relationships with regulators are essential to secure adequate returns on required funding.

As in many sectors, growth through mergers and acquisitions can be a key driver of valuation. Non-regulated services may also enhance financial performance. Large companies may expand by acquisition of small private or municipal entities across the U.S. where greater economies of scale improve performance. Over the

years, non-regulated businesses, such as telemarketing, construction management, public works and military services, and utility billing, have had mixed success. Still, profitable unregulated assets can lift actual returns on investment above those specified by utility authorities.

Water utility stocks are considered conservative with modest risk and largely stable income.

EBJ: What have been some recent major transactions?

Overdorff: In 2020 **KKR**, in partnership with **XPV Water Partners** formed a wastewater treatment platform with the goal of creating the leading provider of end-to-end nutrient management solutions for municipal and industrial wastewater treatment facilities. Through the foundational acquisitions of **Environmental Operating Solutions, Inc.** ("EOSi") and **Nexom Inc.** – two providers of nutrient management technologies – the platform aims to address nutrient contamination of water globally by building a diversified and growing portfolio of leading solutions.

Earlier this year, **Partners Group**, a global private markets firm acquired **Resilient Infrastructure Group**, a water infrastructure platform focused on acquiring, developing, financing and operating distributed water-related facilities in the US and Canada. Resilient is headquartered in Portland, Oregon, and provides distributed water and wastewater solutions to industrial, technology, institutional and municipal clients that solve their site-specific treatment needs. Concurrent with Partners Group's acquisition of Resilient, the Platform closed an investment in a wastewater-to-renewable natural gas project at Threemile Canyon Farms in Oregon.

Another example of private equity investment in the space was the December 2020 acquisition of **Inframark LLC** by **New Mountain Capital**. Inframark is a leading national provider of outsourced operations and maintenance ("O&M") services to water and wastewater treatment facilities for both municipal and industrial customers. The Company is one of four national operators in the water and wastewater O&M space and the only "pure-play"

provider. Inframark has a well-established value proposition that allows its customers to reduce operating costs, stay ahead of evolving regulatory trends, improve quality and EHS metrics, and implement digital solutions.

New Mountain identified Inframark as part of its multi-year deep-dive sector initiatives in sustainability and infrastructure & utility services, which include a specific focus on water services. As a follow-on investment, Inframark acquired **Environmental Development Partners** (EDP) of Jersey Village, Texas in April 2021. EDP provides professional, innovative, and efficient operation services to more than 70 clients in the greater Houston area.

EBJ: How much interest is there in the water industry from the private equity standpoint? Are there certain situations, conditions or opportunities that are attracting investment?

Overdorff: Private equity often leans to fragmented and non-discretionary industries for consolidation plays and small local, regional business and industrial services companies proliferate in the U.S. This is characteristic for companies in the water infrastructure services sector, particularly, outsourced operations and maintenance (O&M) services. It is estimated that there are more than 500 local/regional O&M providers throughout the United States.

The outsourced O&M services industry has seen significant consolidation across larger market participants, many of those have been backed by private equity firms that seek to grow their portfolio companies through M&A. Nationwide providers in the O&M market seek opportunities across the United States and internationally in high-growth and complementary geographies.

The highly fragmented outsourced O&M services market represents a significant opportunity for PE sponsored platform companies to engage in acquiring “bolt-on” acquisitions in a “roll-up.” Identifying targeted geographies for expansion is likely to reveal local outsourced O&M providers seeking capital infusion.

The greater the population density, the greater opportunity for added efficiencies and greater profitability.

Municipalities, privately-owned water & wastewater systems and industrial manufacturers are increasingly utilizing outsourced providers for O&M services that include:

- Water & wastewater distribution and collection system management
- Biosolids management
- Asset management
- Supervisory Control and Data Acquisition (“SCADA”)
- Smart metering
- Customer service and billing
- Factors contributing to the increased utilization of outsourced O&M services and support implementation of cost-savings include:
 - Aging municipal workforce and rising wage rates
 - Increasingly complex operations
 - Increasing regulatory and compliance factors
 - Decreasing emphasis on non-core operations

EBJ: How much is technology driving M&A trends?

Overdorff: Technology is a clear driver for an industry that must do more with less. Automation and data-based management, fast data collection and smart data

transformation is the driving force behind more independent, efficient and sustainable water infrastructure. Industry experts see municipalities increasingly implementing smart, autonomous processes in drinking water and wastewater treatment plants. In turn, sensors will play a key role in improving performance to minimize the effort, time and money tracking leaks. Globally, remote control of all processes will continue to be a priority, from infrastructure operation to the management of work orders for field operators. And finally, in the field of communications, 5G is becoming a tremendous resource.

A recent notable transaction was the **Audax Private Equity** acquisition of **S.J. Electro Systems Inc.** (SJE) in June, 2021. SJE operates globally through seven locations with a worldwide customer base and markets several well respected brands in the highly fragmented water controls market.

EBJ: What are some other trends within the water industry? How have things changed over the past couple of years and how do you think it will be in the next couple of years?

Overdorff: Historically, there has been a chronic, long term and insufficient investment in the nation’s water infrastructure. Billions of dollars have been needed each year to renew and replace outdated pipes, pumps, storage facilities, and treatment plants that ensure clean water delivers to homes and businesses across the nation, carry away and safely treat sewage and stormwater, and return treated water to rivers, streams, and other water bodies.

Alarian Represents Inland Waters on its Sale

Alarian Associates, Inc. represented Inland Waters, Inc. on its sale to Infrastructure Services Group (“ISG”), an investment platform in the water and sewer infrastructure sector, and a portfolio company of Juniper Capital Management, a Dallas-based private equity firm. Inland Waters was founded in 1998 and has a track record of providing specialized pipeline services to clients such as state and local governments, contractors, commercial entities and industrial facilities throughout New England. The company’s services include vacuum excavation, main line and lateral grouting, sewer pipe cleaning, digital inspections, cured-in-place pipe spot repair and reinstatement, lateral inspection, lateral reinstatement, hydro excavation and manhole rehabilitation. The acquisition of Inland Waters fits well with ISG’s geographic and industry focus. Inland Waters will continue operating as a standalone business unit.

Local, state and federal funding is meeting only a fraction of the current need. If this trend continues, the nation's water systems will become less reliable, breaks and failures will become more common, vulnerabilities to disruptions will compound, and the nation's public health and the economy will be put at risk.

2020 laid bare the under-investment as state and local tax revenue shrank and budgets across the board were hit. The Covid-19 pandemic, showcased as recently as late August, the deleterious impact to the nation's clean water supply as residents in Orlando were told to "slow their taps because of a shortage of liquid oxygen used to treat water was required for the treatment of Covid-19 patients."

The nation's population growth has been modest growing only 7.4 percent since 2010. However more than 86% of this growth occurred in urban and suburban areas. This geographic concentration of population growth will require centralized wastewater treatment (WWTP) plants to accommodate a larger portion of the nation's wastewater demand. Further, as the nation's population ages, the work force that has supplied the manpower for operations and maintenance of the US infrastructure is depleted. Additionally, the upward pressure on wages demanded by essential workers suggests that municipal budgets will require more money for projects and payrolls in the future.

EBJ: Alarian represented Inland Waters, Inc. on its sale to Infrastructure Services Group (ISG), an investment platform in the water and sewer infrastructure sector, and a portfolio company of Juniper Capital Management. Can you tell us this transaction?

Overdorff: Based in Johnston, Rhode Island, Inland Waters was founded in 1998 and has a track record of providing specialized pipeline services to clients such as state and local governments, contractors, commercial entities and industrial facilities throughout New England. The company's services include vacuum excavation, main line and lateral grouting, sewer pipe cleaning, digital inspections, cured-in-place pipe spot repair and reinstatement, lateral

inspection, lateral reinstatement, hydro excavation and manhole rehabilitation.

Infrastructure Services Group (ISG) added Inland Waters to a portfolio of water infrastructure service companies in the northeast. They include Mr. Rehab Systems in Mechanicsburg, PA and Green Mountain Pipeline Services, Bethel, VT. Mr. Rehab provides sewer cleaning, inspection and rehabilitation and Green Mountain provides similar services in New England. Combined with Mr. Rehab and Green Mountain, ISG has expanded its geographic coverage in New England and the Mid-Atlantic.

The acquisition of Inland Waters fits well with ISG's geographic and industry focus. Inland Waters will continue operating as a standalone business unit.

ISG recognizes that aging water and wastewater infrastructure systems are challenged by climate change and extreme weather events, increasing demand for rehab and repair.

EBJ: What other services does Alarian provide to companies that operate within the environmental industry?

Overdorff: Alarian is a mergers and acquisitions advisory firm in the lower middle market providing services to both buyers and sellers. The firm advises middle market clients on the sale, merger, or other disposition of their businesses, from early stage strategic planning to final transaction closing. The Company guides clients by:

- Thoroughly evaluating strategic alternatives
- Developing key value drivers of the transaction
- Preparing detailed confidential offering materials
- Identifying and qualifying potential buyers or sellers, domestically and internationally
- Driving the transaction to a successful close

Alarian provides a traditional, hands-on approach to M&A for middle market companies with total enterprise value be-

tween \$10 million and \$200 million that been increasingly served by digital electronic market places. By focusing on the infrastructure segment, Alarian is known in the industry as a knowledgeable, thorough and experienced transaction advisor.

EBJ: Wh at other big deals have you done in the industry?

Overdorff: I served as the M&A advisor to **Clean Earth Inc.**, prior to its acquisition by **Harsco Corporation** (NYSE: HSC) in June 2019. Clean Earth was awarded the 18th Annual M&A Advisors 2019 Private Equity Deal of the Year (\$500M - \$1B). I was also the advisor to Clean Earth for four of its seven acquisitions that fundamentally transformed the business in four years. During those four years, Clean Earth grew from \$25M EBITDA to near \$60M of EBITDA at close. Clean Earth provides essential processing, treatment, disposal and recycling solutions for a wide range of complex, highly recurring waste streams such as hazardous and non-hazardous waste, contaminated soil and dredged material.

These are some other deals we did in the environmental industry:

Disposal and Recycling Technologies, Inc: DART has a RCRA Part B Licensed TSDF in Charlotte, NC and a non-hazardous waste facility in Detroit. We advised Clean Earth on this transaction.

AES Environmental: A handler and processor of hazardous and non-hazardous waste, engaged us to sell the company to Clean Earth, Inc.

EWS: A permitted hazardous waste facility was sourced for Clean Earth, Inc. to build out their hazardous waste processing capabilities.

First Response: We represented the majority owner in a sale to C3 Capital of a controlling equity stake in First Response, an environmental services company.

Enviro-Safe Corp.: We supported the company in a series of transactions, including several acquisitions and a final sale of the company to private investors. ■