

Germany's smart meters market heats up

Alexandra Dockreay

02/11/2016

The upcoming sales of Techem and ISTA, the two dominant German smart metering providers for heat and water, could go for approaching €4 billion (\$4.44 billion) each, and mandated financial advisers are already preparing to launch sale processes for both. It remains to be seen whether both will go out to market at the same time, while a federal inquiry and new technologies could cause further complications.

Deutsche Bank has been hired to advise Australian infrastructure investor Macquarie on the sale of Techem. Techem is owned by Macquarie European Infrastructure Fund 2 (MEIF2), a 2006 vintage fund with its primary term ending in 2018, though it has extension options. MEIF2 acquired Techem for €1.5 billion in 2007.

Market observers are saying that the enterprise value of Techem could be around €3.5 billion and the business reported €744.5 million turnover for the year ending 31 March 2016.

Meanwhile Goldman Sachs is mandated to prepare the auction of ISTA. The owner of ISTA, since April 2013, is private equity firm CVC Capital Partners. CVC holds Techem in Fund V, a 2009 European fund. CVC had first acquired ISTA from German utility E.ON in 2003 for €930 million, before selling a majority stake to Charterhouse in 2007, which it bought back in 2013 in a deal valuing ISTA at €3.1 billion.

Market observers now suggest ISTA could be worth more than Techem, with an enterprise value of €4-4.5 billion. ISTA's revenue was €810.4 million in 2015.

Business models

Both companies manufacture, install and read heating and water smart meters, which allow residents to monitor their consumption. The two have over half their operations in Germany, but are also present elsewhere in Europe, in the UAE and Turkey. ISTA is also in China, Techem also in Brazil.

Their contracted customers are owners of residential apartment blocks or commercial buildings. Landlords take out long-term contracts with Techem and ISTA to install and read the smart meters in the whole building, and then the landlords are entitled to pass on a consumption-calculated cost for each of the end-users, their tenants.

This sub-metering pass-on results in a low likelihood of the landlord shopping around for cheaper deals. Their core sub-metering business exhibits certain characteristics attractive to infrastructure investors: long-term contracts, stable cash flows, low capital expenditure requirements and little customer price sensitivity.

Baker & McKenzie partner Dr. Tim Heitling says, "A difference [between the two companies] is that Techem is also active in the energy contracting sector, which is not a major part of its business but an important part. They provide heating and power solutions for commercial buildings, which could be considered infrastructure-like as well due to the long-term contracts, 10 years or longer, and the integration of combined heat and power plants." He added utilities might be interested in acquiring this unit from Techem's new owner.

Challenges for buyers

International aims of improving energy efficiency generally support the smart metering market but, as Heitling explains, potential bidders for Techem and ISTA are discussing two major challenges facing their core businesses.

One is that the Federal Cartel Office launched an inquiry into the sub-metering of heating and water costs in July 2015, and no announcements or outcomes have since emerged. Rumour is that by year-end there may be some statement, but it is certainly difficult to launch the sale processes of these two dominant companies with the cloud of uncertainty hanging. Heitling says, "There could be different outcomes. One is they start infringement procedures against particular companies, or they could come up with proposals for the legislators to enhance competition, or decide there is already sufficient competition...."

Heitling says the other major challenge centres around technology advances. "{Techem and ISTA} focus on meter readings with respect to heat and water and what could be a risk is the tendencies to move to smart homes or smart buildings with one metering system to optimise the energy balance of that building, including heat, water, electricity and gas. That might impact their businesses, and the new Law for the Digitisation of the Energy Turnaround recently enacted at the end of August 2016 may pose further challenges in this respect."

That law will give tenants greater termination rights upon the contracts between landlords and the heat metering companies, if individual tenants arrange installation of their own combined smart meters.

If electricity and gas utilities move to offer sophisticated, comprehensive smart metering technology they could become major new players competing on heating meters. Germany's Law for the Digitisation of the Energy Turnaround includes a roll out plan for smart meters for high energy-consuming properties from 2017-2032. Techem and ISTA may be able to seize an opportunity to act as third party meter suppliers for electricity and gas utilities.

Bidding candidates

However, Markus Muhs, partner at Clifford Chance, says, "If you look at the existing core business {of Techem and ISTA} there is probably limited potential for growth in home markets. But maybe buyers can look at the international potential..." For example in July 2016 Italy confirmed the compulsory introduction of smart metering for heating in apartment blocks.

Muhs adds, "Pure private equity players who seek to create value within a short period of time may view these companies as too mature. Infrastructure funds could be interested but core infrastructure or institutional investors would need to take a view on the long term perspective. It is hard to tell how the regulatory framework will develop and which role new players will take. The ongoing 'smartification' of the services and digitisation {sic} create both, opportunities and threats for this kind of business."

The two sales are expected to draw a similar crowd, but are each of such a scale that bidders are unlikely to have the capabilities to bid both at the same time. Rumour is that ISTA will go first.

Thank you for printing this article from IJGlobal.

As the leading online publication serving the infrastructure investment market, IJGlobal is read daily by decision-makers within investment banks, international law firms, advisory firms, institutional investors and governments.

If you have been given this article by a subscriber, you can contact us through www.ijglobal.com/sign-in, or call our London office on +44 (0)20 7779 8870 to discuss our subscription options.