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Varcoe: Even with crude prices pulling back, M&A action picks up in Canada's oilpatch with $2.3B deal

'Instead of taking money to drill wells, why not take the money to buy production?'

Chris Varcoe • Calgary Herald
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Roger Tang, CEO of Deltastream Energy Corporation, was photographed in Calgary on Tuesday, May 5, 2020. Gavin Young/Postmedia

The best time to be a seller is when others are flush with cash and looking to buy.

After a string of summertime deals in the Canadian oilpatch — punctuated by news on Wednesday of a $2.3-billion takeover — that basic principle is what Deltastream Energy CEO Roger Tang is counting on, even with the latest pullback in crude prices.

The privately held junior petroleum producer, which pumps out about 20,000 barrels of oil per day in Alberta, is considering its strategic alternatives — including a possible sale, with potential offers expected later this month.

“Certainly, the market is quite hot compared to what I had expected and there are a lot of transactions,” Tang said in an interview Wednesday.

“Even with $95 (crude), it’s still a very healthy oil price and people now are not investing back into the ground, so there’s a lot of free cash flow to acquire assets to expand down the road.

“Instead of taking money to drill wells, why not take the money to buy production?”

Strong oil prices have provided a high-octane boost to industry balance sheets this year, with debt levels plunging and cash flow levels expected to hit record levels.

The M&A market in the sector is also gaining traction.

As Reuters reported Wednesday, Strathcona Resources has struck a deal to buy privately held Serafina Energy, a heavy oil producer with assets in Saskatchewan, for $2.3 billion.

Officials with Calgary-based Strathcona, which is owned by Waterous Energy Fund and Strathcona employees, declined to comment.

However, a research report issued last week by Moody’s Investors Service noted Strathcona agreed to an initial payment of $1.9 billion on the deal closing later this month, and then deferred payments of $100 million in each of the following four months.

Serafina produces about 40,000 barrels of oil per day, mainly from its thermal heavy oil properties in Saskatchewan. The addition will propel Strathcona’s output to about 150,000 barrels of oil equivalent (boe) per day.

Moody’s affirmed Strathcona’s credit ratings and said the outlook remains positive.

“The transaction increases their size and scale and gives them more diversity within heavy oil assets in Canada,” Moody’s analyst Paresh Chari said in an interview.

“The assets themselves are pretty complementary to their existing platform.”

Strathcona has been a consolidator in the Canadian oilpatch over the past three years, snapping up Pengrowth Energy Corp. in 2019 and Osum Oil Sands Corp. the following year. It acquired the Tucker thermal oilsands asset from Cenovus Energy for $800 million last December.

After a quiet start to the year, a series of other M&A transactions in the sector were announced this summer.

Tourmaline Oil Corp. confirmed last week it has agreed to buy Rising Star Resources for $194 million, while Enerplus Corp. announced the $140-million sale of some assets in Alberta to Journey Energy Inc.

On Wednesday, Paramount Resources said it has made a $69-million Duvernay acquisition.

These transactions follow in the wake of two of the year's biggest transactions — before Strathcona's latest move.

In June, Whitecap Resources agreed to buy XTO Energy Canada from joint owners Imperial Oil and ExxonMobil for $1.9 billion, while Cenovus Energy purchased BP's interest in the Sunrise oilsands property for $600 million, along with a contingent variable payment of up to $600 million.

In the first six months of this year, industry M&A activity hit an estimated $4.5 billion, according to data from Sayer Energy Advisors.

The recent flurry of deal-making has been driven by oil prices stabilizing in the range of US$95 to $100 a barrel in recent months, narrowing the gap between what sellers are asking for their properties and what bidders are willing to pay, said Sayer president Tom Pavic.

"Once you see stability, that is when you're able to get transactions done, where buyers and sellers are able to meet," Pavic said.

Commodity prices have been strong this year, although oil markets have dipped recently.

After a surge to start the year following Russia's invasion of Ukraine, benchmark West Texas Intermediate crude prices have dropped from $117 a barrel in early June to close Wednesday at $90.66, down $3.76 on the day.

Fears of a global recession and growing inventory levels have weighed on the market recently. At Wednesday's meeting of OPEC+, the cartel and its allies (including Russia) agreed to increase production in September, but only by an additional 100,000 bpd.

"It's a barely perceptible nod to (U.S.) President (Joe) Biden — and other consumer countries — that have asked OPEC to produce more oil, and they clearly are very reluctant to do that," said Bill Farren-Price, a director at consultancy Enverus Intelligence Research.

While oil and gas markets gyrate, some shoppers of Canadian energy assets have remained patient.

"We are actively looking at things; we've been in several bid processes," said Cardinal Energy CEO Scott Ratushny.

"We don't need to buy anything and I think that seems to be a general consensus in industry now. We've got 10 years' worth of drilling inventory so there's no real impetus to buy something unless it's a good deal."

At Deltastream, Tang is also looking for a good deal for his investors, with bids expected to arrive in mid-August.

The company's high-quality assets in the Clearwater play in northwest Alberta have sparked interest from prospective buyers across North America that was "three times more than I expected," he said.

"We don't have to sell," Tang said.

"If nobody buys us and pays a premium, we will just march on with our five-year plan, but we decided after eight years now, it's a good time to test the market — and the market is relatively strong."

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