

Oil and gas company forced to sell itself at 80% discount ‘canary in the coal mine’ for struggling sector

Value of Alberta energy assets for sale has doubled since last year, but buyers are scarce



A Pengrowth Energy facility in Lindbergh, Alberta. Analyst Jeffrey Craig says the company's acceptance of a five-cent-per-share takeover bid "might be a canary in the coal mine" for companies with unsurmountable debt. *Supplied*



VICTOR FERREIRA

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 Comment

Weighed down by burdensome debt and tightening capital flows, Alberta’s energy sector is looking toward consolidation as a solution, but in a market with few buyers, sellers might have to be willing to take a discount.

According to a report published on Oct. 30 by Sayer Energy Advisors, a Calgary-based broker in the merger and acquisitions space, the value of oil and gas assets that are domiciled in Alberta and available for sale has more than doubled to \$3.7 billion from \$1.8 billion at this time last year. The sudden increase can be attributed to a lack of capital and activity in the sector’s M&A

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had been trading 400 per cent above that level. While the deal hasn't been approved by shareholders, the discount that Pengrowth was forced to take may lead to other firms in similar situations reassessing whether they can continue to demand premiums in M&A deals, according to Veritas Investment Research analyst Jeffrey Craig.

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"I think we are certainly starting to reach a point where this deal might be a canary in the coal mine," Craig said. "A deal of both this size and how strange it was probably resets the bar ... for companies that have debt they can't get out from under."


The Sayer report points to three other publicly traded companies in similar situations. Obsidian Energy Ltd. initiated a "strategic alternatives process" in September, which may result in a sale, merger or recapitalization. Bellatrix Exploration Ltd. has gained court protection from creditors as it also searches for a buyer, while Accel Canada Holdings Ltd. and Accel Energy Canada Limited have filed for the same as they look to enter a restructuring process.

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Acquisitions in the space are typically made by large-cap names such as Suncor Energy Inc. or Canadian Natural Resources Ltd., Craig said, but the lack of interest is no surprise given how shareholders have punished energy companies for making similar purchases in the past.




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Large cap energy investors would predominantly prefer that these companies stay away from mergers and acquisitions for the time being, Portfolio Management Corporation managing director Anish Chopra said.

"The prevailing thought around large cap oil companies is to spend less on acquisitions and ... (more) on stock buybacks to enhance shareholder value," said Chopra, who invests in both Suncor and Cenovus Energy Inc. "It's just better to buy the assets you know the best, which are your own."

Even if this were not the case, energy companies would still have to determine if an acquisition even makes sense strategically, he said. There may be no reason to continue to expand in Alberta at a time that capital is being choked out of the space. Instead, companies may evaluate whether it makes more sense to be aggressive in the U.S. under a friendlier jurisdiction — or in cases like Encana, re-domiciling there.

Consolidation in Alberta energy would actually help the space, AGF Investments associate portfolio manager Mike Archibald said. He suggested that capital would free up if five small cap oil and gas producers, each with an output of 10,000 barrels per day, merged to create larger entities.

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It's a solution that's unlikely to gather support.

"The problem with that is you'd have to collapse four management teams that have to basically say I'll put my hand up and say I no longer want to work in this industry," Archibald said.

The capital markets have forgotten about most of the small cap names in the space, he said. They may no longer even be of interest to the investors who have classically made risky bets on names of this size with eyes on a takeover and a premium that would come with it. Archibald can think of multiple examples in the space that trade for under \$1 and have hundreds of millions of dollars in debt.

“There’s no endgame for them,” he said.

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