Flow of Canadian oil patch deals slows to trickle in second quarter

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The value of Canadian oil patch deals dwindled in the second quarter, but one trend remained dominant: foreign players bailing out the sector.

Exploration and production deals in the period totalled $2.3-billion, according to preliminary figures from Sayer Energy Advisors.

That paled in comparison with a record $33.3-billion in the first quarter, and was less than half the $4.9-billion figure recorded in the second quarter of 2016. It was the smallest tally for a three-month period since the third quarter of 2015, when just $1.2-billion in oil patch mergers and acquisitions were logged.

The figures show how weak oil and gas price forecasts following three years of downturn are forcing major structural changes in an industry that requires high capital commitments and can take years to generate returns. In the case of many of the sellers, it highlights a rush to U.S. shale-oil plays, such as the Permian and Eagle Ford in Texas, where producers recoup their investments quickly. The regulatory environment is often seen as more industry friendly and there has been less of a struggle adding export capacity.

The renewed need for Canadian oil and gas companies to wrestle down debt – some taken on to help fund the big acquisitions of 2017 – is expected to ignite another flurry of asset sales as a way to get balance sheets back in shape, likely boosting the total in the last part of the year.

“If the oil price stays where it’s at for the next six months, there are going to be more and more asset sales. There has to be,” said Martin Pelletier, portfolio manager with TriVest Wealth Counsel Ltd. in

Indeed, several forecasters have recently reduced their oil-price projections, as a worldwide glut and rising production in the United States and Canada weigh on markets. For example, brokerage Raymond James cut its forecast for 2017 to $46.68 (U.S.) a barrel from $51.54, and its 2018 outlook to $45.32 from $52. On Monday, U.S. crude closed up 57 cents at $46.34 a barrel.

Two deals accounted for the lion’s share of the hefty first-quarter deal value: Canadian Natural Resources Ltd.’s $7.3-billion (Canadian) takeover of Royal Dutch Shell PLC’s oil sands business and

Cenovus Energy Inc.'s $17.7-billion purchase of ConocoPhillips Co.'s bitumen operations. (Sayer includes both the equity and assumed debt in deals to arrive at its totals.)

In the most recent quarter, Cardinal Energy Ltd.'s $300-million acquisition of Houston-based Apache Corp.'s remaining Canadian business and MEI Holdings Corp.'s $722-million takeout of Centrica PLC's oil and gas assets, made up sizable chunks of the overall deal value.

Hong Kong-based MEI is among a handful of Chinese firms that have stepped in to fill a void among acquirers of conventional energy assets as other foreign players have either jettisoned their Canadian holdings, or sold down large portions.

The other buyers are domestic players that specialize in various aspects of Canadian oil and gas. Tom Pavic, vice-president at Sayer, said that's an important factor to keep in mind. For each seller there is a buyer, meaning there is still interest in acquiring assets, even if it is largely among homegrown companies.

Cenovus is among those banking on that. As it seeks to reduce debt it took on to fund the buyout of ConocoPhillips's oil sands business, the company aims to sell as much as $5-billion of assets by the end of this year. Concerns about debt against a backdrop of weak oil prices have led to a 46-per-cent drop in Cenovus shares since it announced the deal in late March.

"From an M&A standpoint, I think it's a much better environment from a year ago," Mr. Pelletier said. "From an investor standpoint it's different. But now the big question is, who's the buyer?"

On the financing front, the big acquisitions drove an increase in the first half, especially in debt markets, Sayer's Mr. Pavic said. In the period, the industry raised a total of $17.5-billion and $13.4-billion of that was debt financing. In the first half of 2016, the industry raised $7.1-billion, and equity issues accounted for $6.4-billion of it.

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