Calgary-based energy firms ripe for takeover

Low stock prices fuel suggestions

BY REBECCA PENTY, CALGARY HERALD; WITH FILES FROM STEPHEN EWART JANUARY 19, 2012

Encana Corp., Talisman Energy Inc. and Nexen Inc. are being raised by analysts and investors as the oilpatch players most likely to have targets on their backs in the near term.

Photograph by: Stuart Gradon

When the stock prices of Canada's largest oil and gas companies hover at unsustainably low levels, takeover suggestions start circulating.

Encana Corp., Talisman Energy Inc. and Nexen Inc. are being raised by analysts and investors as the oilpatch players most likely to have targets on their backs in the near term.

"Within the large-cap space, those are the obvious ones," said research analyst Todd Kepler of Cormark Securities Inc.

Investors frustrated by operational setbacks or the strategic direction at each company have pushed stocks low, out of sync with high oil prices tracking more than $100 a barrel, while bargain basement natural gas prices have added to the downward trend.

Though the stocks are cheap, most observers suspect only a national oil company or supermajor has the financial wherewithal to take either of the three Calgary energy firms out with a friendly or hostile bid and few speculate an all Canadian transaction could emerge.

Shares of Canada's top gas producer Encana closed up one per cent Tuesday off a 52-week low of $17.39 the day before, giving the company a market capitalization of 60 per cent of its $22-billion value a year ago.

Talisman is in much the same boat, with shares at $11.58 Tuesday, down from $22.65 the same time in 2011. Shares of Nexen traded down 23 per cent Tuesday from a year earlier.

Leadership missteps at the top have fuelled investor discontent, putting all three potentially in play, said John Stephenson, a partner at Toronto-based First Asset Investment Management Inc. who manages natural resource investments. First Asset, with $2.6 billion in funds under management, is invested widely in Calgary's large energy players, including Encana, Talisman and Nexen.

Low natural gas prices that are helping to push down energy stocks more broadly are creating a value proposition for buyers, Kepler said. The Alberta spot price for natural gas hit its lowest in 26 months last week and U.S. gas futures fared worse on Tuesday.

"There is an opportunity for a lot of companies to reposition in Western Canada or take advantage of companies that perhaps are perceived to be undervalued," Kepler said.

Kevan Holroyd, an associate partner at Ernst & Young in Calgary who advises on mergers and acquisitions, named Encana, Talisman and Nexen as examples of firms with particularly depressed equity valuations among widely discounted Canadian energy firms.

"If you look at it, somebody from afar would think a lot of the companies out there would be vulnerable for a takeover," Holroyd said.

After the departure of Marvin Romanow as chief executive last week at Nexen, Stephenson said the company is "for sure" a potential takeover target that could be acquired by a national oil company for as low as $22 a share, a premium of 17 per cent over Tuesday's close, which equates to about $11.6 billion for the whole company.

Nexen "over-promised and under-delivered" under Romanow, Stephenson said, and faces operational challenges at the company's Long Lake oilsands project, in the North Sea and the likelihood the Gulf of Mexico, where Nexen is drilling, has become a "big boys game" after BP PLC's Macondo spill.

Others have suggested a Nexen takeover bid could come in at $15 billion or more.

Chinese state-owned oil companies increasingly eyeing Canadian energy firms are unlikely to step up to the plate for a deal that large, said Wenran Jiang of the University of Alberta's China Institute, citing both financial and political concerns.

"My sense with talking to senior executives on both sides is the Chinese are comfortable in moving forward in the range of $2-to $3-or $4-billion deals, but I think it would quite a different step to move up to $15-billion plus," Jiang said.

Talisman and Encana could be attractive to an oil major, Stephenson said. He said Talisman CEO John Manzoni shares the blame for the company's low stock price. Since Manzoni took over in 2007, Talisman has diversified too much globally, instead of delivering on Manzoni's promise to focus on North America, the North Sea and Southeast Asia, Stephenson said.

Encana's 2009 spinoff of its oil assets to form Cenovus Energy Inc. under chief executive Randy Eresman was misguided, he added, noting the company is late to the game of drilling for the more lucrative liquids-rich gas over dry gas.

Canaccord Genuity Inc. analyst Phil Skolnick suggested Encana could be acquired by a state-owned oil company because of its low stock price, noting a risk the federal government might block such a foreign takeover, given Encana is "the flagship gas company for Canada."

The question is whether any nearterm takeover bid is welcomed or not, since there are precedents for both in the oilpatch.

For example, Suncor Energy Inc.'s 2009 merger with Petro-Canada was friendly. Talisman's hostile bid for Wascana Energy Inc. was thwarted in 1997 by white-knight Canadian Occidental Petroleum Ltd, Nexen's predecessor company.

"It's more likely to happen on an unsolicited or unfriendly basis among the large caps, because those management teams are unlikely to be cohesive entities like we see in the junior or mid-cap space," Kepler said.

Spokespeople for Encana and Talisman declined to comment on takeover suggestions and Nexen did not return a request for comment.

Romanow said at a December investor day that Nexen and advisers had examined "every possible path to generate some value" for investors last year, including selling the company, shedding assets and buying back stock.

The company decided instead to deal with the "cause" of lack of confidence in Nexen, he said, performance at Long Lake.

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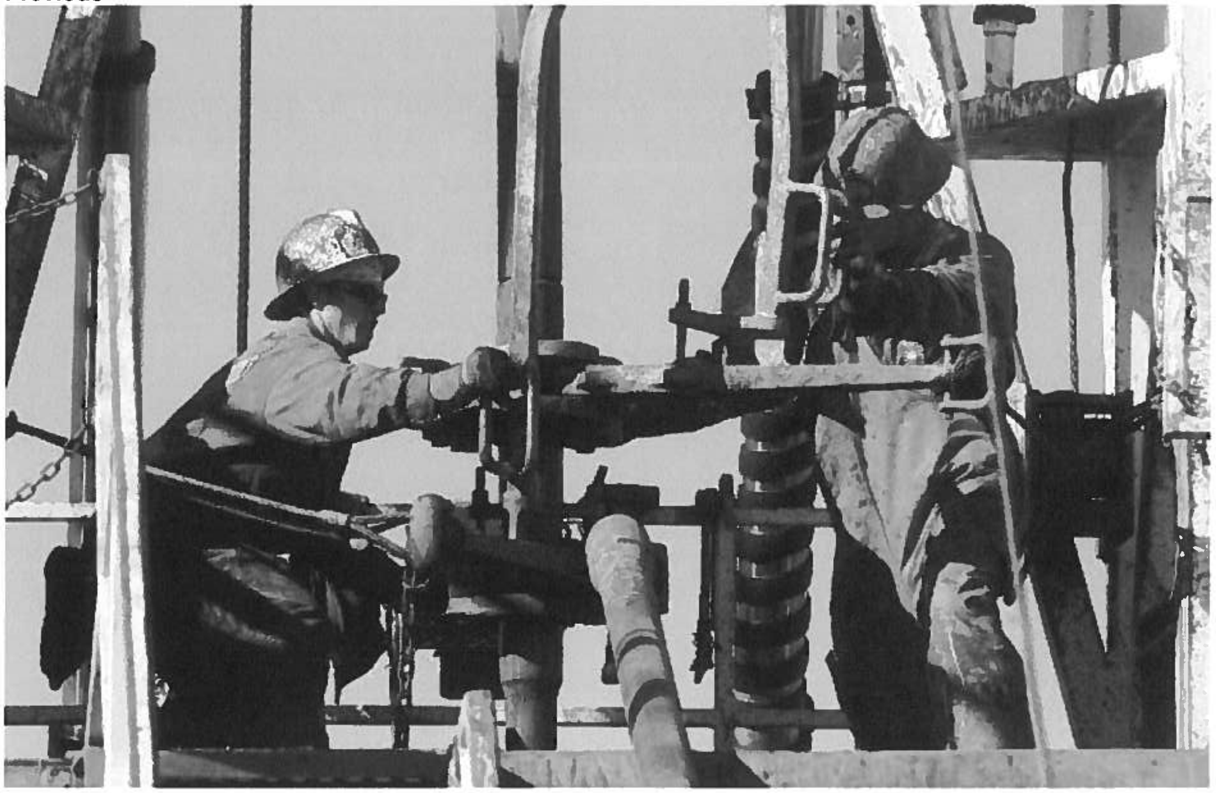
Previous Next



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