



## Can Talisman Energy Inc. Bounce Back?

### Description

Stronger industry fundamentals and the share prices of Canadian energy companies lagging behind their U.S. counterparts have attracted the attention of institutional investors and Wall Street.

**Talisman Energy Inc.** (TSX: TLM)(NYSE: TLM) was lauded as a deep-value investment opportunity when iconic activist investor Carl Icahn unveiled a 6% stake in the company in July 2013.

But Talisman continues to face considerable hurdles in rebuilding its balance sheet, divesting itself of poor quality assets and unlocking value for investors, leaving many to question whether Talisman can ever bounce back.

### What are the key problems facing Talisman?

The majority of Talisman's problems can be traced back to its range of geographically diversified assets, many of which are of questionable quality and are heavily weighted to lower-margin natural gas.

Key among these assets is Talisman's mature North Sea assets, which continue to be a significant drag on the company. The poor quality of these assets can be seen by the low margin or operating netback for oil and liquids, which for Q2 2014 was \$14.02 per barrel.

This is compared to the oil and liquids netback of \$41.67 reported by Talisman's North American operations and the \$43.69 per barrel by its South East Asian operations for the same period. These netbacks are roughly triple those of its North Sea operations.

Furthermore, crude production from the North Sea continues to remain flat, down by 6% quarter-over-quarter and unchanged year-over-year for Q2 2014.

This low netback along with Talisman's heavy production weighting to lower-margin natural gas, which made up 61% of total second-quarter production, continues to weigh heavily on the company's overall performance.

For the same period its company-wide netback was \$27.18 per barrel, which is significantly lower than

many of its peers, because their production is more heavily weighted to higher-margin light oil and natural gas liquids. At the end of the second quarter, **Husky Energy Inc.** (TSX: HSE) reported a netback of \$48.70 per barrel, while **Crescent Point Energy Inc.** (TSX: CPG)(NYSE: CPG) reported a massive netback of \$54.75 per barrel.

The company is also now set to sell its oil and gas assets in Iraqi Kurdistan due to growing unrest in the region.

The divestment of non-core assets continue to impact Talisman's financial performance with cash flow plunging 23% quarter-over-quarter and remaining relatively flat year-over-year for the same period. This saw Talisman report a net loss of \$0.24 per share for the quarter, which was well below the consensus analyst estimate of \$0.06 per share.

### How much is Talisman worth per share?

Talisman's oil reserves have a net present value after income taxes and the application of a 10% discount rate of \$11.9 billion or \$11.53 per share or equivalent to the company's current share price, indicating the company is fairly valued.

But there have been a number of analysts who believe Talisman is worth up to \$17 per share if the company is able to divest itself of its troublesome North Sea assets and unlock the value of those assets in North America, Asia, and Colombia.

However, in order to realize the full value of its assets, Talisman may need to be broken up, with the sum of its parts worth more than the company as a whole. This could be a likely scenario with suitors including Spanish integrated energy major Repsol SA circling the company seeking to acquire Talisman's high-quality North American or Colombian assets.

Clearly Talisman is in trouble and while Icahn's investment may have inspired confidence in some investors, the company's performance continues to be dragged down by its North Sea operations.

For all the reasons discussed, now may be the time for investors to take a backseat and watch how things play out for the remainder of 2014, with Talisman set to make further divestments and Repsol looking to acquire assets.

### CATEGORY

1. Investing

### TICKERS GLOBAL

1. NYSE:VRN (Veren)
2. TSX:VRN (Veren Inc.)

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**Author**  
mattdsmith

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