# Why Investors Should Decline the Takeover Bid for Pacific Rubiales Energy Corp.

## Description

The news for investors in beleaguered oil explorer and producer **Pacific Rubiales Energy Corp.** (TSX:PRE) continues to worsen. The recent collapse in oil prices couldn't have come at a worse time for the heavily indebted oil producer. Not only did its profitability decline, but there are fears it could breach its debt covenants due to sharply low earnings caused by significantly weak oil prices. Now, Mexican conglomerate **Alfa SAB,** along with partner **Harbour Energy Ltd.,** has pitched a low-ball takeover bid for Pacific Rubiales, valuing the company at far less than what it is truly worth.



**Now what?**

Alfa, which owns 19% of Pacific Rubiales, is the single largest shareholder in the company, and in conjunction with Harbour Energy, has offered to purchase all available common shares for $6.50 each. This values Pacific Rubiales at $6 billion including debt, and I believe it represents a fraction of Pacific Rubiales' true long-term value.

It was only a year ago when crude was trading at over US$100 per barrel that Pacific Rubiales was hovering around $18 per share, almost triple the current offer.

Even more startling is that after factoring in the value of Pacific Rubiales' independently assessed oil reserves, its interests in exploration properties, pipelines and other infrastructure, and then deducting its debt of US$4.7 billion, I have calculated it is worth about $15 per share.

Surprisingly, despite the current bid being just under half of this amount, Pacific Rubiales' board have announced that they support the offer. This is even more extraordinary considering that there is no takeover premium attached to the bid, and that Alfa needs an oil operator like Pacific Rubiales if it is to participate in energy auctions in Mexico as planned.

However, the reasons for this support could be due to the number of headwinds that Pacific Rubiales is currently facing. These include the impending loss of its working interest in the Piri-Rubiales field in June 2016. This interest accounts for 41% of its total oil production and a fifth of its oil reserves, meaning its loss will have a significant impact on its asset value and financial performance.

Furthermore, Pacific Rubiales' attempts to acquire and develop other oil assets to replace this production have been mediocre at best. Then there is the threat that it may breach its debt covenants, and the likelihood of this occurring increases the longer crude prices remain discernibly low.

Nonetheless, given the low-ball nature of the bid it is not surprising that a group of Venezuelan investors, who have acquired more than 11% of Pacific Rubiales shares, are opposing the bid and making it clear they won't sell their stake to Alfa; they view Pacific Rubiales as a long-term investment opportunity and the bid is well below what it is truly worth.

**So what?**

If recent statements by management are to be believed, Pacific Rubiales is well positioned to weather the current storm in crude prices. It has a range of levers available to manage its debt position and the loss of the Rubiales field. The current low-ball bid is certainly is not in the interest of existing shareholders other than Alfa, particularly if you believe that crude prices will recover some time soon.

**CATEGORY**

1. Energy Stocks
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1. TSX:FEC (Frontera Energy Corporation)



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mattdsmith