Why Crescent Point Energy Corp. Should Be Applauded

Description

On Tuesday **Crescent Point Energy Corp.** (TSX:CPG)(NYSE:CPG) announced a deal to acquire **Legacy Oil Plus Gas Inc.** (TSX:LEG) for $563 million. Crescent Point will also take on Legacy's debt of nearly $1 billion.

This may not please Crescent Point's shareholders. The company will be financing the transaction entirely with new shares—about 40 million in total—which could put a lot of pressure on its stock price. As of this writing, the shares are down 5% on Wednesday. But make no mistake, Crescent Point is doing exactly what it should be doing. Below we look at three reasons why.

1. The price is right

Usually takeovers come with a rich premium, but this is an exception. The deal values Legacy at $2.85 per share, or just 4.6% above its average trading price over the last 30 days. In fact, Crescent Point is getting a discount on Legacy's last closing price. So, why did Legacy's board agree to this?

Well, to put it mildly, Legacy has struggled in this low oil-price environment. Its stock price sunk by 64% in 2014 alone. Making matters worse, Legacy backstopped a $5.7 million margin loan for CEO Trent Yanko, which the board was heavily criticized for. In April an activist investor announced his intentions to add three new directors to Legacy's board.

So, it seems that Legacy's board members simply have had enough. And that's great news for Crescent Point, which is getting an excellent deal. To put this in perspective, the company is paying (including debt) about $70,000 per flowing barrel of production. By comparison, Crescent Point trades at over $100,000 per flowing barrel.

2. There's a strategic fit

Crescent Point isn't just getting a good deal. It's also buying a company that complements its existing business.

This is mainly because the bulk of Legacy's assets are in southeast Saskatchewan, an area where

Crescent Point has a big presence. Thus, Crescent Point should be able to achieve some cost savings.

Furthermore, because Crescent Point has a strong balance sheet, it can fully afford to exploit Legacy's assets. Before the transaction, Legacy didn't have enough money to fully develop its own properties.

3. The balance sheet remains pristine

Long-time Crescent Point shareholders should be used to this kind of transaction by now. The company is well known to finance acquisitions with new shares, something that is often frowned upon by value investors. But it comes with one major advantage: the balance sheet has always remained rock solid.

Let me put this another way. If some of Crescent Point's larger acquisitions in the past were financed with debt, then this kind of deal may not have been possible. So, today at least, the company deserves a pat on the back. And if I were a Crescent Point shareholder, I would expect more deals like this to come.

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Date
2025/09/09
Date Created
2015/05/27
Author
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