



Does Pacific Rubiales Energy Corp. Now Have Over 100% Upside?

Description

When **Alfa SAB** and **Harbour Energy** teamed up to offer \$6.50 per share for **Pacific Rubiales Energy Corp.** (TSX:PRE), the price seemed quite fair. After all, Pacific Rubiales had been struggling mightily, and its shares had traded for as little as \$2.54 in April. And the company's board unanimously accepted the offer.

But there was also fierce opposition. Leading the charge was O'Hara Administration Co., which owns nearly 20% of Pacific Rubiales. Proxy advisors Glass, Lewis & Co. and Institutional Shareholder Services Inc. were also recommending that shareholders reject the deal, claiming it undervalued the company.

In the end, that opposition proved to be too much. On Wednesday Pacific Rubiales announced that Alfa and Harbour have withdrawn their bids. Clearly, there was far too much opposition to the \$6.50 offer.

Here's the bad news for Pacific Rubiales shareholders, including O'Hara: there weren't any higher bids. So, in response to the news, the company's shares have sunk by roughly 40% as of this writing.

But if you don't own any shares, this may look very tempting. After all, some prominent shareholders claim this company is worth more than \$6.50 per share, and you can buy a stake for less than \$3.20 per share.

Is this the opportunity of a lifetime?

To answer this question, let's take a look back to where Pacific Rubiales was before the offer. Unfortunately, it did not look good. Most notably, the company had more than \$4.4 billion of net debt on its balance sheet, a massive number for a company currently worth less than \$1 billion.

Making matters worse, Pacific Rubiales had recently learned its contract to operate Colombia's oil field won't be extended beyond June 2016. That contract currently provides about 30% of the company's production.

Pacific Rubiales has reacted swiftly in this environment. It slashed its capital budget by over 50%, and renegotiated its debt covenants. The company is also furiously cutting costs, and is planning asset sales.

But it may not be enough. The oil price has fallen once again, and now sits barely above US\$50. There are reasons to fear it may fall further. If this happens, then Pacific Rubiales's debt may be too much to overcome.

A very leveraged bet

There's a good possibility that Pacific Rubiales shares will soon be worth zero. But if things go right for the company, there's a lot of upside for its stock price.

To put this in perspective, the company trades at about \$35,000 (including debt) for every daily barrel of oil production. That's not a bad price at all, even when factoring in the canceled Colombian contract.

At the end of the day, this is very much a hit-or-miss bet. Investors will likely either double their money (or perhaps more), or lose everything. So, if you're thinking of jumping in, just make sure not to commit too much money.

CATEGORY

1. Energy Stocks
2. Investing

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1. TSX:FEC (Frontera Energy Corporation)

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