



## Is Canadian Oil Sands Ltd. Being Too Greedy?


### Description

When **Suncor Energy Inc.** ([TSX:SU](#))([NYSE:SU](#)) launched a bid to acquire **Canadian Oil Sands Ltd.** (TSX:COS) it was clearly being opportunistic in its approach. Canadian Oil Sands's stock had been hammered over the past year as persistently weak oil prices, along with its debt-laden balance sheet, sent its stock down by more than 65% before Suncor made an offer.

However, in not only outright rejecting, but now fighting that deal, Canadian Oil Sands is walking a fine line because the fact of the matter remains is that it still has a lot of debt and negative cash flow. In other words, it might be getting a little too greedy.

### Numbers don't lie

As the chart below shows, Canadian Oil Sands's net debt has ballooned to more than \$2 billion since the onset of the downturn.

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As a result of this ballooning debt, Moody's downgraded its credit rating to one notch above junk, specifically citing the deterioration of the company's balance sheet. Further, it pointed out that the company was expected to generate negative cash flow of \$125 million over the next 15 months that would also largely be funded by more debt. That would likely trigger another credit downgrade, this time to a junk rating.

This lack of cash flow fueled whispers in the market place that the company was looking for alternatives such as selling its future production in order to bring in some cash. While the company quickly shot down those rumours, the fact remains that it's struggling under the current oil price. It's a price that has yet to show too many signs of improving. In other words, if oil prices do stay lower for longer, Canadian Oil Sands will only continue to struggle.

### A tale of two companies

Suncor Energy, on the other hand, is generating almost as much cash flow now as it was when oil

prices were higher. In fact, it's generating so much cash flow that it has a surplus on its balance sheet. That's why the company said it was on the lookout for acquisitions. Further, CEO Steve Williams specifically said that he was looking for an opportunity to acquire assets in a fire sale brought about by low oil prices.

That's exactly where we find Canadian Oil Sands. It's a company that has too much debt for the current oil price, and is running an unsustainable business if the current oil price is the new normal. Further, if oil prices were to really collapse (some are warning that \$20 per barrel isn't out of the question), that would put Canadian Oil Sands on precarious footing.

There's a growing risk that it might not survive if a wave of bankruptcies sweep through the energy sector, which is a growing risk if oil remains weak and credit starts to tighten.

### **Investor takeaway**

There's no denying that Suncor Energy is making an opportunistic offer to acquire Canadian Oil Sands as the company has been waiting patiently for the opportunity to go shopping for assets at fire sale prices.

However, given Canadian Oil Sands's rising debt levels, and the fact that oil prices might not recover for a while, this might just be the best offer the company receives. It's running a real risk of being too greedy at a time when its financials are deteriorating. If oil prices take another leg down, or credit really tightens in the sector, the company might regret fighting to remain independent.

### **CATEGORY**

1. Energy Stocks
2. Investing

### **POST TAG**

1. Editor's Choice

### **TICKERS GLOBAL**

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2. TSX:SU (Suncor Energy Inc.)

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