



Is Canadian Oil Sands Ltd. Headed Back to \$6 Per Share?

Description

Shareholders of **Canadian Oil Sands Ltd.** (TSX:COS) have a tough decision to make.

Back on October 5, **Suncor Energy Inc.** ([TSX:SU](#))([NYSE:SU](#)) stirred up the oil patch when it launched a hostile takeover bid for Canadian Oil Sands.

At the time, the \$6.6 billion all-stock offer represented a 40% premium to the pre-bid closing price of Canadian Oil Sands shares. The rise of Suncor's stock in the past month now puts the premium above 50%.

Canadian Oil Sands rallied from \$6.20 to above \$10 on the news, but has fallen back in recent days as WTI oil takes a new run at \$40 per barrel.

While investors try to determine if a better deal could be in the cards, a war of words is heating up between the two companies.

Canadian Oil Sands says the bid vastly undervalues the business and its resources. Suncor says the offer is fair given the current state of the oil market and the underperformance of the assets.

What is at stake?

Canadian Oil Sands owns a 37% stake in the Syncrude oil sands project. Suncor is also a partner with a 12% position.

Syncrude has been an operational nightmare for several years, and while the project is coming to the end of a major capital program, production costs still remain very high and output is struggling to meet the facility's design capacity.

When oil traded for \$100 per barrel, the inefficiencies were easily covered by high margins, but the collapse in crude prices has put Canadian Oil Sands in a precarious financial position, and that is why Suncor is trying to take it out.

Canadian Oil Sands reported Q3 2015 cash flow from operations of \$82 million and spent \$84 million on capital expenditures, so the business is still cash flow negative. The company also handed out \$25 million in dividends during the quarter.

Long-term debt is \$3.6 billion. Most notes are not due before 2019, so the company isn't at risk of a default for the next three years, but oil has to recover if Canadian Oil Sands is going to survive.

Should shareholders reject Suncor?

The Suncor bid is good until December 4, so there is still some time for another suitor to enter the game, but oil prices are on the slide again and no white knight has even hinted (publicly) at having an interest in Canadian Oil Sands.

Suncor apparently tried to do a friendly deal at a higher price earlier in the year, but Canadian Oil Sands didn't want to dance. Now that oil prices look like they could be in the dumps for longer than previously expected, the stakes are a lot higher for Canadian Oil Sands and its shareholders.

Pundits have speculated that **Imperial Oil Limited** could come to the rescue because it holds a 25% position in Syncrude and has the contract to operate the facility. That might happen, but you would think Imperial Oil would have already stepped up to the plate by now, especially if Suncor has been pressuring Canadian Oil Sands to sell for several months.

At this point, the \$10 per share that shareholders could have gotten a week ago is looking pretty good. If Suncor walks, Canadian Oil Sands could easily fall back to the \$6 mark.

There is no doubt the long-term value of the resource base is probably a lot higher than the price Suncor wants to pay, but Canadian Oil Sands shareholders will never see the benefit of that potential if the company doesn't survive the rout.

I think Suncor or a combination of Suncor and the other Syncrude partners will eventually buy Canadian Oil Sands, but hoping for a better offer looks risky right now.

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