Should Canadian Oil Sands Ltd. Accept the Offer From Suncor Energy Inc.?

Description

Canadian Oil Sands Ltd. (TSX:COS) has had more than its fair share of trouble this year.

The company has seen revenues and profits dry up as commodity prices have plummeted and taken the loonie down along for the ride. If that weren't bad enough, shareholders have also seen dividends dry up and a mountain of debt emerge.

And finally, the inaction by the company to make a deal in yet another potential takeover deal has shareholders scratching their heads in astonishment.

Hostile takeover or knight in shining armour?

Suncor Energy Inc. (TSX:SU)(NYSE:SU) is a company at the other end of the spectrum. It has invested a lot of money in making processes more efficient and, as a result, is able to turn a profit even with the unfavourable price of oil.

It's no secret that Suncor has been hoarding cash, waiting for the opportune moment to snatch up a competitor that is going through rough times (and there's quite a few of them to choose from). That moment came a few weeks ago, when Suncor made a $6.9 billion all-share bid for Canadian Oil Sands. The offer resulted in Canadian Oil Sands's price spiking by 55%. There has been no response to the offer as of yet; both companies seem to be waiting to see who will blink first.

For shareholders of Canadian Oil Sands, the waiting game continues. The company is holding out and likely hoping for a better offer. Suncor, on the other hand, has been firm in stating that the offer is more than fair, and adding to it now would only be a "premium on top of a premium."

Worse still for Canadian Oil Sands would be if Suncor were to drop out and move their war chest on to another target. The gains that Canadian Oil Sands has made in recent weeks would be erased and troubles would continue.

Suncor's letter to shareholders

Suncor clearly wants Canadian Oil Sands to make a decision and even sent a very frank letter to shareholders this week with the headline “Hope is not a strategy.” The letter goes on to state the following: “Canadian Oil Sands shares have recently been trading at around $10. ‘Doing nothing’ carries the very risk that Suncor’s offer goes away and the value of your shares could fall back towards their pre-bid level of just over $6 a share.”

But wait! There’s more:

“You will be left holding shares in a company which has demonstrated negative free cash flow, about $2.3 billion in debt that is already just one notch above ‘junk’ status, and a strategy based almost entirely on hope–hope that oil prices will rise and hope that Syncrude will sort out its ongoing operational challenges.”

If nothing else, the Suncor letter painted the harsh reality for shareholders and was about as blunt as it could be.

If you are a shareholder of Canadian Oil Sands, you are hoping the deal goes through while the premium is still reflected in the stock price. There really aren’t any better options or suitors that could come to rescue, and commodity prices don’t seem likely to increase to the point where Oil Sands will be reaping huge revenues. If the deal falls apart or if Canadian Oil Sands rejects it, expect the price to tumble back down to $6 or possibly even lower.

Suncor, which has also seen an increase in share price, currently trades at just over $37, while Canadians Oil Sands is trading at $9.34. This is the third and likely final attempt at a takeover by Suncor, and the deal expires on December 4.

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Date
2025/08/03
Date Created
2015/11/14
Author
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