The Profit Opportunity With Canadian Oil Sands Ltd.

Description

When **Suncor Energy Inc.** (TSX:SU)(NYSE:SU) made a hostile $4.3 billion bid for **Canadian Oil Sands Ltd.** (TSX:COS), it was widely seen as a low-ball offer. One of Canadian Oil Sands's largest shareholders, billionaire Seymour Schulich, even called the bid “ridiculous” and “a no-ball offer.”

Most investors seemed to agree. Canadian Oil Sands shares actually traded at a premium to Suncor’s offer, meaning investors were confident a higher bid would come, either from Suncor or from another company.

Fast forward to today and the story is completely different. Oil prices have continued falling with the WTI price down by more than 20% since Suncor launched its takeover attempt. Canada’s most debt-ridden oil producers have seen their share prices crash. And Canadian Oil Sands now trades at about a 7% discount to Suncor’s offer.

So how exactly should investors react? Is there an opportunity here?

Canadian Oil Sands has only one way out

With oil prices falling so dramatically, it should be clear by now that Canadian Oil Sands should accept the offer. After all, the company is now burning cash, and the balance sheet is a major concern, too. Canadian Oil Sands is also unlikely to draw a higher bid.

And one must remember that COS traded at $6.18 per share before Suncor’s offer. That’s 24% below today’s share price. And if Canadian Oil Sands rejects the bid, then its share price will likely fall even further given the state of the oil markets.

The profit opportunity

If you’re feeling adventurous, there’s certainly a profit opportunity with Canadian Oil Sands. Assuming the company’s shareholders accept Suncor’s bid, then you would make roughly 7% (based onSuncor’s current share price). You would also make this money relatively quickly, since Canadian OilSands’s poison pill expires in early January.

The risk is too great

At this point, Suncor’s bid is probably going to be successful, simply because Canadian Oil Sands shareholders have too much to lose. But you should still avoid the shares for a couple of reasons.

First of all, the bid is far from a done deal. It requires two-thirds of Canadian Oil Sands shareholders to accept the offer, and Mr. Schulich owns a 5% stake. Secondly, the downside scenario is simply far too scary, even if it’s an unlikely outcome.

So your best bet at this point is to sit back and watch this whole drama play out. It will be very entertaining for all of us as long as we keep our distance.

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