Alimentation Couche-Tard Inc.: 1 Deal Too Many?

Description

Alimentation Couche-Tard Inc. (TSX:ATD.B) admitted Tuesday that it was in talks to acquire **CST Brands Inc** (NYSE:CST), the convenience store spinoff of **Valero Energy Corporation**, an independent U.S. refiner of more than two million barrels of oil per day.

While CST's stock has done well since its May 1, 2013, spinoff and is up 56% through August 16, the company undertook a strategic review in March to find ways to enhance shareholder value. One of those possibilities is to sell itself to someone with the resources to pay upwards of US$5.2 billion. Couche-Tard is clearly the leading candidate to make the deal.

But should it?

Motley Fool contributor Demetrius Afxentiou has already touched on some of the problems a potential deal would create for Couche-Tard at the Competition Bureau in Ottawa. I won't retrace his steps, but suffice it to say, Couche-Tard will likely have to sell some locations in Atlantic Canada, Quebec, and possibly even Ontario.

CST's Canadian operations generated US$114 million in operating income in 2015 on revenues of US$3.4 billion. With 869 locations in CST's Canadian operation (303 selling fuel and merchandise), Couche-Tard would ultimately get some of the purchase price back by selling off some of these locations; the tough part could be finding a buyer.

That's the first problem.

The second concern is CST's 19.3% stake in **CrossAmerica Partnership LP** (NYSE:CAPL), a whole distributor of motor fuel in 20 U.S. states as well as an operator of 40 convenience stores in West Virginia. Analysts expect U.S. regulators won't look approvingly on a foreign entity exercising any type of control over CrossAmerica's business. That stake would likely have to be sold as well.

This brings us to the third problem: debt.

As of the end of fiscal 2016, Couche-Tard had net debt of US$2.2 billion, or one times EBITDA. Assuming it pays no premium to current prices, it should need approximately US$2.8 billion in debt to complete the deal along with the assumption of another US$1.8 billion from CST. With CST's trailing 12-month EBITDA of US$523 million, Couche-Tard's leverage would go from one times EBITDA to 2.5 times EBITDA after completing the transaction.

That puts its leverage at a level not seen since the **StatOil ASA** acquisition in 2012.

The good news: Couche-Tard management are seasoned pros at integrating acquisitions and trimming debt. While this one's got a few more regulatory hurdles to jump through on both sides of the border, once it's sold off the necessary locations and CST's interest in CrossAmerica, that leverage ratioshould be much closer to historical norms.

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