Cenovus (TSX:CVE) Acquires Husky Energy for $3.8 Billion

Description

On October 25, **Cenovus Energy** (TSX:CVE) announced it will acquire **Husky Energy** (TSX:HSE) in an all-share transaction valued at $3.8 billion. Husky closed trading at $3.17 on October 23 indicating a market cap of $3.2 billion.

Cenovus said the acquisition will create an integrated oil and natural gas company with an "advantaged upstream and downstream portfolio that is expected to provide enhanced free funds flow generation and superior return opportunities for investors." The combined entity will have an enterprise value of $23.6 million and will operate as Cenovus Energy.

Cenovus claimed the acquisition will be accretive to all shareholders on cash flow and free funds flow per share with expected annual rate run synergies of $1.2 billion. It expects free funds flow break-even at WTI (West Texas Intermediate) pricing of US$36 barrel in 2021 and at less than US$33/bbl by 2023.

The acquisition will create Canada's third-largest oil and gas producer with a total production of 750,000 barrels of oil equivalent/day (BOE/d). Further, Cenovus believes stable cash flows will support its investment-grade credit profile allowing it to pay a quarterly dividend of $0.0175 per share.

Husky shareholders will receive 0.7845 of a Cenovus share plus 0.0651 of a Cenovus share purchase warrant in exchange for each Husky common share.

Why is Cenovus optimistic about the acquisition?

Cenovus expects the combined entity will have low exposure to Alberta's oil pricing while maintaining a healthy exposure to global prices. It will allow the entity to integrate the low-cost oil sands and heavy oil assets infrastructure with extensive midstream and downstream operations.

The diversified portfolio of energy assets will enable the company to generate a predictable revenue stream across price cycles, allowing it to have an efficient cost structure and robust liquidity.

It will now be the second-largest Canada-based refiner and upgrader with total North American upgrading and refining capacity of 350,000 bbls/d. It will also have access to 265,000 bbls/d of current takeaway capacity on major pipelines and 305,000 bbls/d on planned pipelines. Further, Cenovus will now have 16 million barrels of crude oil storage capacity.

Annual free funds flow of $1.2 billion

Cenovus expects to generate an additional $1.2 billion of annual free funds flow which consists of $600 million in annual corporate and operating synergies and $600 million in capital allocation strategies.The cost-saving will be achieved via reductions of the workforce and overhead costs that include streamlining of IT systems.

Cenovus confirmed, “Immediate efficiencies are also expected to be realized by implementing best practices from each company, including applying Cenovus’s operating expertise to Husky’s oil sands assets, leveraging the increased portfolio’s scale in the Deep Basin, and pursuing commercial and contract-related efficiencies on midstream marketing and blending opportunities.”

The combined entity is expected to sustain production levels and downstream operations with annual capital investments of $2.4 billion which is $600 million lower per year on a standalone basis.

Further, the free funds flow generated will help the entity to achieve a net-debt-to-adjusted-EBITDA target of less than 2 in 2022. The acquisition is expected to close in the first quarter of 2021 after which Cenovus will hold a 61% share in the combined entity, while Husky will own 39%.

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