Falling Markets and Canadian Exits Illustrate Transaction Activity in the Oil and Gas Sector

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The following is an adapted summary of data provided in Stikeman Elliott LLP’s Canadian Oil & Gas 2017 Annual Review.

Overview

2017 was another turbulent year in the oil and gas sector. The regulatory and economic climates for oil and gas continued to shift quickly throughout the year, as many oil and gas entities found themselves balancing cautious optimism with the realities of a continued commodities slump. Notwithstanding the fact there were a few mega-deals in the industry in 2017, the total number of deals as well as the overall values for them were down nearly across the board when compared to 2016. This was a somewhat surprising occurrence given the upward trend in the economy generally from Q1 to Q4. We have reviewed the major acquisition and finance transactions in the sector and have summarized the deals and trends for the past year in comparison to 2016.

Trends in Mergers & Acquisitions

There were only six public upstream M&A deals in 2017 (against 17 in 2016), and two of those were for companies listed in Canada with assets located entirely outside of Canada. Deal value declined by 45%. In large measure this reflected a 12-month period in which most companies saw their share prices sell-off from the beginning of the year to the end. Falling markets do not easily give rise to consolidation in the upstream sector.

Private upstream M&A for assets was much more active, with a total deal count up marginally from last year and total value up about four times over last year. However, the general tone of the activity by value was strongly biased towards exiting Canada. ConocoPhillips, Shell, Centrica, Qatar Petroleum and Apache all completed major sales of Canadian assets, while Cenovus and Canadian Natural increased oil sands exposure in two deals worth just over $30 billion. Those two transactions alone accounted for about 80% of all private M&A activity by value. Without those deals, private upstream M&A declined by value in 2017.

Cenovus’ acquisition of the ConocoPhillips assets led it to become a seller in four of the 10 private M&A deals worth more than $300 million, as it sought to absorb its new holdings. Pengrowth also completed a major disposition program, selling four separate packages, each worth more than $150 million.

In the midstream sector, the market was very quiet. There was one large public deal (Pembina’s acquisition of Veresen) but private deal value declined by about 80%.

In services, there was meaningful consolidation in the public market, where there were five deals (about three times last year by value). All of those deals involved the merger of Canadian-based providers with other Canadian-based companies. Consolidation works for some. In the private market activity was very slow – deal count was down about 50% from last year. In part this reflects the bias of the survey, which captures announcements by public companies of their private acquisitions. That market remained very slow as companies turned away from acquisition-led growth.

	2017 Deal Value (CAD millions)	2017 Deal Count	2016 Deal Value (CAD millions)	2016 Deal Count
Mergers and Acquisitions				
Upstream				
Public Targets	$3,004	6	$5,455	17
Private Targets & Assets	$38,423	48	$9,000	49
Midstream				
Public Targets	$9,300	1	-	-
Private Targets & Assets	$1,088	7	$6,530	10
Downstream				
Public Targets	$68	1	-	-
Private Targets & Assets	$1,600	1	-	-
Oilfield Services				
Public Targets	$882	5	$265	2
Private Targets & Assets	$182	5	$530	11

Trends in Finance Transactions

In relation to finance transactions, the single most important number in our survey may be that upstream equity prospectus offerings fell by about 50% from 2016, both in value and number. The endless bearish trade in equity capital markets kept issuers firmly at home.

There were only six upstream prospectus deals for proceeds of more than $100 million in 2017. Cenovus topped the list in equity, raising approximately $3 billion in the spring in connection with its acquisition of the ConocoPhillips assets. The rest of the capital was directed at oil sands (MEG Energy), yield-oriented oil producers (Cardinal Energy and Whitecap Resources), Montney growth (Painted Pony) and the Bakken (PetroShale). The message was pretty clear. Canada didn't warrant much equity energy capital.

Upstream private placements of equity saw a similar decline in value, but maintained activity by number. The largest deals were split between companies focused on oil and gas development in Western Canada

(Karve Energy, Whitecap Resources and Delphi Energy) and companies conducting exploration and development activities outside of North America (SDX Energy, ShaMaran Petroleum and Oronova Energy).

A handful of upstream issuers were able to find fairly ready access to the debt markets. Debt deals were up 13% by number and about 3.5 times by value. The list reveals that deal flow was very concentrated. At the top of the list was Canadian Natural, which led the field with six deals for total proceeds of just under $5 billion.

Most of the big players in the midstream sector were active in the equity markets, but deal count was down by 23% (or 20% by value). The largest deals were completed by AltaGas (an acquisition financing) and Kinder Morgan Canada (an IPO), but Enbridge, TransCanada, Keyera and Pembina Pipeline all sold common or preferred shares. Enbridge did four of the 12 debt deals for total proceeds of $3.5 billion.

Services finance was basically flat in 2017, but total debt proceeds were up about 300%. Outside of the STEP and Source IPOs there was only one other equity deal worth more than $100 million.

Sponsors were active in the upstream sector. There were 13 publically-announced deals with sponsors, including three deals led by AIMCo.

	2017 Deal Value (CAD millions)	2017 Deal Count	2016 Deal Value (CAD millions)	2016 Deal Count
Finance Transactions				
Upstream				
Equity (Prospectus)	$4,389	16	$8,650	42
Equity (Private Placement)	$956	31	$2,000	35
Debt	$14,036	29	$3,140	16
Midstream				
Equity (Prospectus)	$7,880	10	$9,805	13
Equity (Private Placement)	$1,900	2	$145	1
Debt	$7,118	12	$5,715	9
Downstream				
Equity (Private Placement)	$668	2	-	-
Debt	$500	1	-	-
Oilfield Services				
Equity (Prospectus)	$572	10	$675	9

Equity (Private Placement)	$142	5	$305	4
Debt	$2,089	8	$690	3

Future Outlook

Regulatory uncertainty for Canadian oil and gas entities has thus far continued well into 2018. Canadian oil and gas entities continue to struggle getting their product to new markets and competing with the swelling shale energy industry south of the border. Canadian exits and consolidations may yet continue while equity investment remains sluggish. However, cautious optimism has crept into the industry. There are signals of sustained growth in global oil markets and renewed interest in Canada's natural gas markets. We eagerly await to see if fortunes will turn in the second half of 2018.

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