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HD **Oil slump spurs wave of merger deals**

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MORE than $13 billion of oil and gas deals announced last week have bankers around the world hoping a wave of energy sector mergers and acquisitions spurred by sliding oil prices is building quicker than thought.

The $US8.3bn ($10.2bn) takeover of Canada's Talisman Energy by Spanish major Repsol , the cashed-up Woodside Petroleum finally buying some growth through $US2.75bn worth of stakes in Chevron LNG projects and Cooper Energy's low-cost entry into a Santos-owned Bass Strait oilfield have all been helped by an oil price that has slumped 50 per cent in the past six months.

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The threat of sustained lower oil prices is putting pressure on companies with high debt or capital commitments, and the longer prices stay down, the greater the need is for asset sales or mergers to strengthen balance sheets. At the same time, cashed-up buyers will be able to get better prices, both because the oil outlook has crashed and because some sellers' need for funds is becoming more urgent.

But offsetting any merger and acquisition surge in the short term will be boards' reluctance to sell as the oil price is sliding. To overcome this reluctance, either an acceptance the price outlook has changed for the worse and oil won't bounce back, or increased balance sheet pressures will be needed.

For Woodside chief Peter Coleman , who has been under pressure to find growth projects to spend ample LNG cashflows on, the sliding oil price is finally providing the chance to flex a strong balance sheet after he walked away from a couple of deals this year because he couldn't get the right terms.

"We think we're actually entering a window that Woodside's been waiting for the last three years," Coleman said on Tuesday after signing a deal to buy US-based Apache's 13 per cent stake in the $29bn Wheatstone LNG project and 50 per cent stake in the not-started Kitimat LNG project in British Columbia.

More purchases up to $5bn could be on the way for Australia's biggest stand-alone oil company.

"We've been preparing ourselves — our cash commitments are low and we have a huge amount of optionality in our balance sheet," Coleman said.

Brent oil prices have slumped to under $US60 on a combination of weaker demand, increased US and Libyan supply and a landmark decision by Saudi Arabia to keep its oil flowing to protect market share, instead of pulling back output to protect prices.

Ernst & Young 's head of Oceania oil and gas transactions, Roger Dartnell, says the time is ripe for Australian acquisitions.

"Given the current market conditions, exploring the ASX for acquisitions is potentially a cheaper and also a more certain way to grow reserves and should be considered by management teams," he says. "Historically a commodity price shock can be a pre-curser to M&A activity — this is a time to be prepared to buy, refinance or defend." Many are pointing back to the late 1990s and early 2000s, when oil prices that slumped as low as $US11 a barrel saw some of the biggest deals in history: Exxon merging with Mobil, Chevron buying Texaco and BP taking out Amoco and Arco.

But any big step up in acquisition activity is not expected in the early part of next year, with some tipping the initial effect will actually be a lull.

"Collapsing oil prices are throttling the M&A market as deals under way are being shelved and would-be buyers are melting away," Wood Mackenzie analyst Fraser McKay says. "Hopeful sellers will not get the offers they would have expected just a few months ago." But the respected consultancy is tipping 2015 will throw up distressed sellers and other opportunities for cash-rich buyers. So for companies with strong balance sheets that believe in long term oil prices of $US80 a barrel or above, 2015 could be a year to make acquisitions.

"Large-scale (global) corporate consolidation may be closer than it has been at any point since the late 1990s," McKay says.

Still, those in the M&A game are not seeing large-scale corporate takeovers in Australia, with asset sales viewed as the main game.

Santos is seen as the big local company whose share price has fallen the most below value. Shares are down one-third since November 26, when OPEC (led by Saudi Arabia) announced its decision not to cut production.

But potential international buyers could be deterred by project risk on the $US18.5bn Gladstone LNG project, which is seen as short of gas and has the added risk of coal-seam gas being an untested large-scale LNG source.

Woodside and Papua New Guinea-focused Oil Search, with strong cashflow and lack of capital commitments, are both down less than 10 per cent since the OPEC decision, meaning there is little chance of someone getting them on the cheap. But Oil Search could still be a target for a bigger player keen to expand into Asian LNG.

US-listed InterOil, a PNG-focused explorer seen as a potential Woodside target, is off 20 per cent this month, so it could be becoming more appealing for Coleman, who has previously said PNG was too expensive.

Potential targets are likely to be those whose share prices have slid because they have, or are seen to have, too many capital commitments or too much debt, as was the case with Talisman.

"The recent drop in oil prices is especially affecting companies that have high financial leverage and negative free cashflow … the Talisman share price has been affected by this," Repsol chairman Antonio Brufau said after the takeover was announced.

"We decided to move forward with this acquisition in the right moment, when we saw a short-term disconnect between the financial markets and the long term value of Talisman's assets." In Australia, the mid-tier and smaller companies are where more value might be seen, as was the case with Chinese companyFosun International 's $500 million takeover of Roc Oil in August.

Other potential targets for buyers with a bullish outlook include Central Petroleum , whose shares are down 60 per cent in the past month, Horizon Oil, off 35 per cent, Tap Oil, off 23 per cent and DrillSearch, off 30 per cent.

Santos has moved to strengthen its balance sheet by cutting capital expenditure and flagging asset sales. It last week announced its first sale, agreeing to sell a 50 per cent stake in the Sole gasfield in Bass Strait and the Patricia Baleen gas plant at Orbost to Cooper Energy for the funding of $50m of project studies.

While the deal had been in progress for a few months, the changing market forces no doubt helped the buyer.

"It's a good time to do a deal," Cooper managing director David Maxwell said. "Where else could you find 100 petajoules (of gas resources) for $27.5m, it's a lower price than exploring and it gets to the market quickly." For Santos and its $8bn market value, the deal is minute. But it cuts a potential $600m spend developing the project in half and will put to use spare capacity in its gas plant.

At the junior end, there are some interesting tussles.

Neon **Energy** and MEO Australia in November agreed to a merger of equals to create a cashed-up junior capable of making up to $50m acquisitions.

But the cash is being targeted by others, with Neon the subject of a proportional takeover from Perth investors Evoworld. The Evoworld bid was defeated last month, but Evoworld has come back and scheduled a January meeting when fewer shareholders are likely to vote.Neon chairman Alan Stein, who co-founded London-listed mid-cap Ophir **Energy** , says the falling **oil** price would be good for the merged MEO-Neon strategy of buying assets. “If the logic was good then, it’s even better now,” he said. “I think this is going to be the best merger year in **oil** and gas since 2002 or 2003.”

CO bpo : Repsol Oil & Gas Canada Inc. | wodpet : Woodside Petroleum Ltd | enpl : Repsol SA

IN i1 : Energy | i13 : Crude Oil/Natural Gas | i1300003 : Crude Petroleum Extraction | iextra : Natural Gas/Oil Extraction

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