Upside in the Energy Downturn

Surprising opportunity arises amid downturn in energy prices

One thing is certain in North America’s energy industry today: not a second goes by that anything is certain. Anybody who is even remotely associated with the energy industry already knows it can be a roller coaster ride. The recent downturn in oil prices at the end of last year into 2015 has made that clear again – and continues to do so. Look a little closer, however, and there appears to be more opportunity than some may think in various surprising places from low energy prices.

For all that has been trumpeted in the media about the crushing impact of low oil prices – and there’s no doubt the impact is very real in different ways – what lies beneath to those who see it and live it as innovative entrepreneurs is the chance to reorganize. It just may produce much bigger results for the long haul. The short term, after all, has never truly reflected the longevity of the energy industry.
Moving forward from the usual predictions, forecasts, guesses and prophecies that always seem to cover the same territory, the most entrepreneurial and innovative companies and business leaders are tapping into new opportunities arising out of the current economic environment.

“When things get tough, there are positives that come out of that,” says Christine Fisher, the Global Practice Leader for Natural Resources and Energy for global executive search firm Stanton Chase International.

“It’s all about opportunities and the upside of the current reality.”

The Lure of New Prospects

The highs of oil prices well above $100 a barrel West Texas Intermediate (WTI) during the summer of 2014 soon became a distant memory as prices began to slide. At the same time, merger and acquisition activity heated up. It was a record year with $63 billion US invested in M&A deals in Canada by the end of December – quadruple the value of deals in 2013, according to Infomart, a division of Postmedia Network Inc. That was slightly more than the value of deals in 2009 amid the global financial crisis of about $62 billion US.

The trend appears to continue in 2015. “Large-scale corporate consolidation is taking place,” confirms Fisher, who has a view on the ground of what’s happening in the industry across North America.

Talisman Energy is one such prominent example. In February this year, shareholders voted almost unanimously – 99.36 per cent – in favour of the $13 billion deal with Spanish energy giant Repsol to acquire all outstanding shares of the company. It had been struggling for some time and the deal reflects the appeal of such companies for acquisition.

It is also a trend that extends to some of the junior oil and gas companies, which have been reduced by half in numbers over the last five years, says Fisher. Many existing juniors, meanwhile, have worked hard to find “creative ways” to weather lower energy prices and the reduced availability of capital so they can remain in business until prices pick up.

M&A activity has clearly been largely driven by commodity prices over the years as a general trend. This year is turning out to be no different. Top executives with successful track records are being tapped by investment banks to review new deal opportunities.
Low cost operators with a strong balance sheet like Tourmaline Oil are now taking advantage of asset sales by big rivals and plan to pick up more. While being selective, prudent and opportunistic, Crescent Point Energy added $1 billion to its line of credit, readying itself for an energy buyers market. A final decline in prices might set up one of the best buying opportunities for energy stocks since the first quarter of 2009.

**Opportunity Knocks**

Some projects have been delayed in the wake of lower prices, cost reduction programs have been implemented and labour costs are being closely managed. An important distinction can be made, however, when it comes to the long-term oil sands projects pushing ahead (others shelved) versus tight oil drilling activity, which has suffered.

Suncor Energy Inc., Canada’s largest oil and gas company, may have announced $1 billion in cuts to its capital spending program for 2015, yet it forges ahead on its massive $13.5-billion Fort Hills oil sands mine and its Hebron project. It has even attracted investment interest recently from the likes of Warren Buffet.

Despite cuts, it plans to spend between $7.2 billion and $7.8 billion CDN in 2015, of which $4.3 billion will be allocated to growth projects. Both Fort Hills and Hebron are expected to come online in 2017.

Fort Hills alone will ramp up to produce 180,000 barrels per day, in conjunction with project partners Total E&P Canada and Teck Resources Ltd. Suncor’s total production in 2015 will average 540,000 to 585,000 barrels of oil equivalent per day, up slightly from 2014.

Oil sands projects and tight oil from fractured horizontal wells weather low oil prices in much different ways. Fisher believes executives, therefore, approach them in uniquely distinct ways, as well. Oil sands operations require huge sums of upfront investment and operate on long-term trajectories; able to continue to be profitable at lower oil prices around $50 per barrel than tight oil projects, which may be questionable even at $80 per barrel by some industry estimates.

Reorganization and restructuring – including top executive talent, along with major projects and spending programs – are playing a vital role in today’s energy environment. “The reaction is optimistic right now,” says Fisher.
“When prices start to fall, it makes executives reevaluate risk and opportunity, but it’s their nature to be pioneers, prospectors and explorers.”

Even service companies are taking action to offset decreased demand by finding ways to improve their services, expand their client base and generally increase their market offering, she adds.

“Business leaders are looking at making changes to key positions or restructuring – either their organization or their talent,” Fisher notes. “You always need strong executive leadership, but when the market returns you’re going to see companies investing money in their people.” The same need applies to current circumstances as people reorganize and restructure, she adds.

One common thread among many companies in all parts of the industry is technology. Many industry-leading energy companies describe themselves as technology companies as much as they do oil or gas companies. “Innovation and technology both play big roles,” Fisher says.

Leaders who understand the increasing role technology will play in the industry are those who stand out the most and also those who will make their businesses thrive with new investments to improve efficiencies in 2015.

Low Oil Prices Lift Key Sectors

Among other key markets for Stanton Chase are the expanding industrial, consumer products and technology sectors. Low oil prices, coupled with global currencies that are lagging against the strong-performing U.S. dollar, have helped boost those sectors. North America’s automotive industry, for example, could set new sales records in 2015, according to some industry watchers. Consumers are saving money at the pump and the appetite for new vehicles grows with those savings in the pocket. Every 10-cent-per-litre drop in gasoline prices adds $5 billion into consumers’ bank accounts. Fleet buyers, such as utilities and government organizations, are also able to invest more.

The technology sector is meeting increased demand for efficiencies by the energy and other industries, while consumer products has become its own world fuelled by the global nature of the economy and emerging market demand.
Leaders Navigate the Roller Coaster

The world consumes about 93 million barrels of oil a day and that consumption is growing. The majority of top industry executives across North America have seen low oil prices many times before. History has shown that periods of a downturn in energy prices doesn’t last long, which makes it a prime opportunity to invest and make key business decisions.

Since 1986, when oil prices dropped by about 60 per cent, it took about six months before they returned to previous levels. In 1999, there was a longer period of up to two years before prices recovered. After the 2008-09 economic collapse oil prices actually returned to near-normal levels within six months. It’s a lesson not to make hasty business decisions based on assumptions that oil prices will remain low for an extended period.

The most successful executives and business leaders understand this.

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Christine Fisher leads the global Natural Resources and Energy practice at Stanton Chase including oil & gas, energy services and infrastructure. She focuses on CEOs, board directors, financial leadership and executive management in operations, engineering, exploration and human development. Christine has led successful client engagements in North America, Latin America, the Middle East, India, Europe, Australia and SE Asia.