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Deal Dynamics
Insights on cross-border M&A
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Stable oil price helps energy and natural resources top all other sectors by M&A value in Q3 2018

- Energy and natural resources attracted the highest cross-border deal value of all sectors in Q3 2018 (US$71.2bn)
- Deal value is up 54% compared with same period in 2017
- Deal volume is 21% below the average quarterly deal volume since 2010 (101 deals)

When Norwegian energy giant Statoil changed its name to Equinor in March, chair of the board Jon Erik Reinhardsen said: “The world is changing, and so is Statoil. The biggest transition our modern-day energy systems have ever seen is underway, and we aim to be at the forefront of this development.” And, from the growth in renewables to the increasing influence of private equity (PE) and investment funds, it is change that is driving M&A in the energy sector.

Energy and natural resources attracted the highest cross-border deal value of all sectors in Q3, counting US$71.2 billion-worth of transactions. This sits 43% above the average quarterly deal value since 2010 and marks the highest quarterly value since Q3 2016.

At the same time, volume fell from 110 to 101 deals between the second and third quarters – 21% below the average quarterly deal volume since 2010. However, it is worth noting that this split between rising value and falling volume is a trend that is occurring across the majority of sectors.

Oil price uptick spurs confidence

The renewed confidence in the M&A market correlates with a continued recovery in oil price. Crude oil prices climbed above US$70 a barrel in January for the first time in three years, double the US$35 all-time low of two years ago. It has increased further to just over US$80 a barrel at the time of writing.

Subsequent earnings growth is enriching companies that have an agenda for change. Energy businesses and investors are seeking to repurpose their portfolios to incorporate high-growth renewables as well as bringing on board shale gas assets. In addition, cash-rich PE firms have entered the field and become serious contenders of prize assets.

Shale on sale

In these transformational times for the energy sector, shale represents a huge opportunity for the industry's super-majors, many of which have seen their crude reserves fall as they made budget cuts to long-term projects during the two-year oil price depression.

United States shale, a young industry, remains highly competitive and flourished amid low prices as it achieved increasingly efficient production and lower costs. Oil output from seven major shale formations in the United States is expected to rise by 79,000 barrels per day (BPD) to 7.6 million BPD in October, according to the U.S. Energy Information Administration.

The shale "boom" convinced British giant BP to spend US$10.5 billion buying a world-class portfolio of US shale gas assets from BHP, in the second largest deal of the quarter. The BHP assets comprise 1 million acres of prime land in the epicenter of shale output, the Permian Basin in west Texas. Shale production in the Permian Basin is expected to double to 5.4 million barrels per day between 2017 and 2023, according to research group IHS Markit. This surpasses output from all other producer nations besides Saudi Arabia and Russia, and clearly demonstrates the rationale for BP's landmark acquisition.

Renewables push

As companies worldwide transition to a lower-carbon system, a rise in M&A activity is also taking place within the renewables sub-sector.

After a strong Q2, deals in the renewable sector were slower in Q3 but noteworthy nonetheless.

For example, Danish firm Orsted, the largest offshore wind farm developer in the world, acquired Lincoln Clean Energy, a leading non-utility developer of wind projects in the United States, for US$580 million. This follows Orsted's divestment of its upstream oil and gas assets to UK firm Ineos for more than US$1 billion last year, which signified a full exit by the company from oil and gas and transformation into a purely renewables focused energy company.

Meanwhile, the largest renewables deal of the quarter saw PE firm Global Infrastructure Partners (GIP) take a 50% stake in UK-based offshore windfarm Hornsea 1 for US$5.9 billion.

The sector is clearly energizing PE groups. With dry powder at record highs, funds are investing across the spectrum. On the back of major deals in the first two quarters of the year, including Chrysaor's acquisition of three North Sea oilfields from Spirit, the third quarter has continued to produce intriguing cross-border buyouts. Alongside the aforementioned GIP transaction, Italian firm F2i SGR agreed to acquire solar energy company RTR Rete Rinnovabile from UK firm Terra Firma for US$1.5 billion.

Traditional deals

Despite these changing times, traditional oil and gas deals still play a major part in energy M&A and will do for the foreseeable future.

Indeed, the largest cross-border deal of Q3 involved a target operating in the natural gas space. A Hong Kong consortium (including CKI Infrastructure Holdings, Power Assets Holdings and CK Asset Holdings) agreed to pay US$13 billion for APA Group, an Australian gas pipeline infrastructure company. However, the proposed transaction is contingent upon receipt of Australian regulatory approvals. Having now been cleared by Australia's competition authority, it is expected to face scrutiny in obtaining Foreign Investment Review Board clearance, on national interest grounds and domestic gas pricing issues.

Moving into the final quarter of the year, a continuing recovery in the oil price will be a crucial factor in determining cross-border dealmaking confidence within the sector. Alongside traditional oil and gas transactions, the three emerging deal drivers – renewables, cash-rich funds and shale prospects – could push the energy M&A market to new heights – especially at the top end of the market.

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