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Weak pound, share-price declines boost bid prospects for U.K. mid-market oil groups

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As equity market valuations and the pound remain depressed following the U.K's vote to leave the European Union, analysts at Liberum Capital Ltd in London believe that mid-market oil and gas companies could soon find themselves in the crosshairs of resource-hungry Chinese acquirers.

They name the most likely targets as Premier Oil plc, Ophir Energy plc, Genel Energy plc and Tullow Oil plc, citing independently operated assets and the likely lack of political or regulatory obstacles, given the companies' relative modest size.

Oil and gas companies have been among the beneficiaries of the U.K's vote to leave the European Union, as some investors have favored real assets while others have bet on a recovery in commodity prices. Large cap oil and gas companies notched up share-price gains this year, with shares in both BP plc (BP) and Royal Dutch Shell plc having gained more than 30% since Jan. 1.

However, shares of mid-market companies Genel and Ophir are still nursing double-digit losses for 2016 while, in the last 12 months, all four companies named by Liberum have suffered double-digit declines. Tullow is the largest of the potential takeover candidates, with a market value of £2.1 billion ($2.8 billion). Ophir was worth about £494 million, as of Friday afternoon in London, while Premier Oil was worth £366.5 million and Genel £333.4 million. All four stocks were down between 1% and 2% on the day, towards the end of the Friday trading session.

Meanwhile the pound is hovering near a 31-year low against the dollar and was recently down 0.91% at $1.3222.

A key source of M&A interest is likely to come from China, according to the analysts. As of Friday about £99 billion ($131 million)-worth of outbound Chinese deals worldwide have yet to close, a record high, according to Liberum.

Without naming likely acquirers, they cite the declining renminbi as incentivizing further capital outflows and expect that rising demand for commodities oil will spur demand for international producers over time.

Oil and gas bankers from London-based Hannam & Partners LLP recently said that if oil prices were to fall again, banks may begin to scrutinize balance sheets across the sector more closely. That in turn could limit funding for the companies, making those with good upstream assets more likely to fall prey to Chinese buyers.

Analysts at Liberum cite operational control over assets and responsibility for investment decisions as key contingents for Chinese acquirers to be interested.

Premier Oil declined to comment on whether it expects to see any approaches but highlighted that the board would be obliged to consider them. Messages seeking comment were left with Ophir Energy, Genel Energy and Tullow Oil.