



FEATURE

# Potash Corp. of Saskatchewan Shares Could Rally on Firmer Fertilizer Prices

Shares of the potash producer could rally as fertilizer prices stabilize. They sport a generous 5.8% yield.

By  
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Fertilizer stocks have been caught this year in the commodities downdraft, and are looking particularly malnourished. Shares of [Potash Corp. of Saskatchewan](#) (ticker: POT), one of the world's largest fertilizer producers, have fallen 26%, to \$26.01, as investors worry about slowing global demand for the company's products. The slide has left the shares trading for just 12.9 times next year's expected earnings, while the dividend yield has ballooned to 5.8%.

Yet, even as fertilizer prices have been crunched, Potash continues to produce considerable free cash flow, giving it ammunition to boost the payout or acquire another company to boost its market share. If prices stabilize in the next year, as expected, the stock could rebound sharply.

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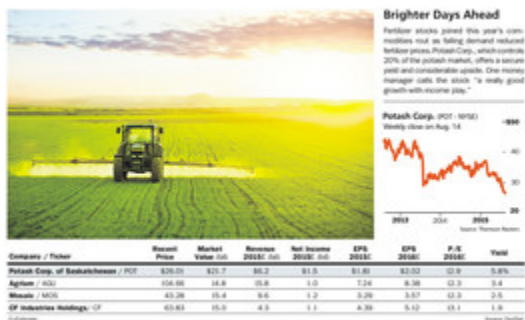


Photo: CactuSoup/GettyImages

Jeffrey Zekauskas, an analyst at JPMorgan, thinks that Potash could be worth \$34 a share by the end of next year, based on a multiple of 10 times expected 2016 earnings before interest, taxes, depreciation, and amortization, versus a current multiple of 7.9. The company's replacement value, he says, is \$52 a share.

**John Petrides, a portfolio manager at Point View Wealth Management in Summit, N.J., has been buying the stock for client accounts. "In an environment where yields are compressing and people are looking for income and for value, here's a really good growth-with-income play," he says.**

**To buy the Potash story, he adds, investors don't have to believe that fertilizer prices have bottomed, only that "we are closer to the bottom than the top."**

Potash Corp. was founded in 1975 and is based in Saskatoon, Saskatchewan. The company is named for its most profitable product, a potassium-based fertilizer it lifts out of mines in Canada and other parts of the world. Potash Corp. also produces nitrogen and phosphate, two other fertilizers that help farmers grow more food on less land, but potash accounts for 57% of gross profit. The company controls about 20% of the global potash market.

Potash's revenue and income have declined for three years on the drop in fertilizer prices. But analysts expect results to stabilize this year and begin to rebound in 2016. Earnings per share are set to rise from an estimated \$1.81 in 2015 to \$2.02 in 2016. In the longer term, earnings could grow at a high-single-digit rate; Morningstar's Jeffrey Stafford sees earnings rising 9% annually for the next five years.

Fertilizer prices have fluctuated in the past few years. Potash, whose price has long been controlled by cartels based in Canada and Russia, peaked above \$800 per metric ton in 2008, as prices for agricultural products rose and producers kept supplies tight. But the subsequent economic slump and resistance from customers sent prices below \$400 by 2009. The Russian cartel broke apart in 2013, sending prices lower again. Potash recently traded at about \$300 a metric ton on the spot market.

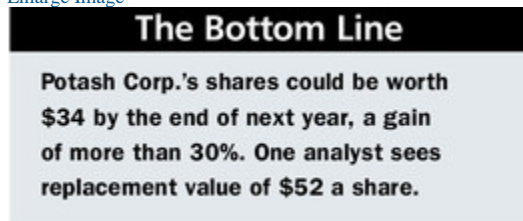
Analysts see less downside from here. The major producers that control the potash market have remained disciplined since the Russian cartel fractured, holding back production to keep prices higher. "A lot of the structural advantages that come with a cartel have been maintained," says Stafford.

**WITH PRODUCTION RELATIVELY STEADY**, the market could eventually benefit from rising demand. Fertilizer demand has fallen this year in North America as farmers cut back due to low prices for corn and soybeans. But Potash has enjoyed higher demand overseas, including in China

and India. On the company's second-quarter earnings call, CEO Jochen Tilk said "Asia in general has been very strong."

In the longer term, Potash has several opportunities for growth. The company has spent the past several years expanding its Canadian mines to allow it to produce more potash. That \$8 billion project is nearly complete, and analysts expect free cash flow to climb to \$1.7 billion in 2017 from \$1.2 billion this year as capital expenditures decline.

[Enlarge Image](#)



Potash might spend some of that cash on acquisitions; it offered \$8.6 billion last month for German fertilizer company [K+S](#) (SDF.Germany). Potash executives weren't available to discuss the deal, but Tilk said on the earnings call that it would help Potash diversify its products and markets.

Analysts are conflicted about the deal; Stafford thinks the price is too high, at a 57% premium to K+S' average stock price in the previous year. But he and others think Potash's balance sheet is strong enough to fund the deal and the dividend.

A growing global population and the structure of the market will make Potash shares attractive in the longer term, Petrides asserts. "You have a handful of fertilizer suppliers and a finite resource with high barriers to entry," he says.

Those dynamics could offer investors a bountiful harvest.

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