

Investors in Fertilizer Stocks Should Remain Cautious This Week

Description

The past few quarters haven't been easy on investors in the fertilizer industry. They've seen their stocks tumble in the aftermath of turmoil in nutrient markets, and the recovery has been painfully slow. This week could again put fertilizer stocks to test as heavyweight **PotashCorp** (TSX: POT)(NYSE: POT) kicks off the earnings season with its first-quarter report.

PotashCorp's earnings are among the most-awaited events in the fertilizer industry. That's because its earnings report holds valuable insight into the future of the overall industry, since the company deals in all three key nutrients – potash, phosphate, and nitrogen.

Unfortunately, given the headwinds in the industry, PotashCorp's earnings report could be a harbinger of tough times ahead. So whether you're an investor in **Agrium** (TSX: AGU)(NYSE: AGU), **Mosaic** ([NYSE: MOS](#)), or any other fertilizer company, you need to fasten your seat belts this week.

PotashCorp may sound hopeful...

All eyes will be on PotashCorp's outlook for its namesake nutrient market, which was rattled last year after Uralkali walked out of the Belarusian Potash Company marketing group. The dust hasn't settled yet – Uralkali's plans are unknown, potash prices are still too low to help producers' profit, and key market India has slashed potash subsidies further this year, which could hurt demand substantially.

Given the backdrop, any positive news or guidance from PotashCorp, even if it's small, could push its shares up, especially since the company's first-quarter numbers will likely disappoint. Analysts estimate PotashCorp's Q1 earnings per share to drop a whopping 45% year over year, backed by 20% lower revenue. PotashCorp's views could also affect Mosaic shares, since the company derives nearly 35% of its sales from potash nutrient. Agrium has least exposure to potash nutrient among the three companies, which also explains why its shares didn't crash like those of peers last year.

...but challenges are aplenty

The problem is that it isn't just the potash market that could've landed on soft patch last quarter. Earlier this month, Agrium dealt a huge blow to investors' hopes when it said it expected to just break even on earnings per share in its first quarter. The guidance was a far cry from Street estimates, and Agrium largely blamed the delayed start to spring planting in the U.S. for lower-than-expected sales.

Given that most fertilizer makers rely heavily on the North American market for revenue, Agrium's projections don't bode well for the industry in general. And if PotashCorp confirms the weakness during its upcoming earnings call, it could send fertilizer stocks lower.

Pressure from all sides

Companies that produce nitrogen have two additional challenges to deal with this year – corn acreage in the U.S. is expected to dip, and natural gas prices have firmed up considerably compared to last year. While corn is the most important nitrogen-consuming crop, natural gas is the key input for nitrogen fertilizer. So that's a double whammy for nitrogen companies.

PotashCorp could have a hard time, since it gets a third of its sales from nitrogen. Agrium [isn't a pure fertilizer](#) player, but nitrogen makes up the greatest portion of its fertilizer portfolio, which in turn accounts for roughly a quarter of the company's total sales. In fact, a weaker nitrogen market was a key factor behind Agrium's muted first-quarter guidance.

Things look equally bleak for phosphate nutrient, which is also Mosaic's primary revenue driver. According to PotashCorp's latest market data report, March potash exports from the U.S. fell 39% year over year, resulting in higher stockpiles. With demand for the nutrient from global markets drying up, phosphate prices could remain under pressure. PotashCorp's upcoming earnings report should shed light on the future of the phosphate market. That could also give Mosaic investors a good idea about what to expect when the company reports its earnings in May.

Foolish bottom line

As the world's leading fertilizer producer, PotashCorp's views hold water. A disappointing set of numbers from the company this week may take a toll on peer stocks as well, but investors should focus on PotashCorp's updates and outlook about the key nutrient markets. If the company sounds cautious, you know you should be too as an investor in the fertilizer industry.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:MOS (The Mosaic Company)

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