Potash Corp./Saskatchewan Inc. Crashes: Is it Time to Buy or Dump the Stock?

Description

Shares of fertilizer giant, **Potash Corp./Saskatchewan Inc.**(TSX:POT)(NYSE:POT) have dropped nearly 11% over the past couple of days, extending its losing streak to a point that could panic investors. The stock has hit its 52-week low and is now down nearly 31% year-to-date.

Does this fall signal the beginning of an extended bear run for Potash Corp., or could this be a golden opportunity to scoop up shares in the company?

What triggered the fall

Negative news has hit the potash industry from all sides this week. The slowdown in China is terrible news for commodities markets; China's Purchasing Managers' Index, a key gauge of the level of economic and manufacturing activity, slipped to a six-year low in September.

Why should Potash Corp. worry about what's going on in China? As the largest potash consumer, China usually sets the benchmark for the prices that potash producers fetch from their contracts worldwide. Aside from concerns about the slowdown in the economy, China is also sitting on huge potash stockpiles. Combined, the two factors could send potash prices tumbling.

Latest industry projections already look scary. Analysts at Macquarie Group have pegged next year potash prices to slump to US$254 tonne. That's 15% lower than current prices and less than half of 2012 potash price levels.

To make matters worse, one of the larger potash producers and Potash Corp.'s peer, **Mosaic,** just slashed its potash production target for the year, citing lower-than-expected demand from key markets in North America and Brazil. Mosaic's cautious potash guidance was one of the biggest factors that sent Potash Corp. shares tumbling this week.

Where does all this leave Potash Corp. investors?

It's obvious that weakness in potash market bodes ill for the company, especially since the nutrient is also the largest contributor (a little more than 50%) to its gross margin. However, one look at Potash

Corp.’s cost profile tells us that the company may be able to reap good margins even in low-potash-price situations.

Potash Corp.'s Presentation at the Scotiabank Fertilizers & Chemicals Conference

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With Potash Corp. keeping its cash production cost for potash well below US$100 per tonne, there’s enough room to earn profits even if its average selling price slips to US$250 a tonne. By focusing on its low-cost facilities, Potash Corp. expects to reduce its production costs by another US$20-30 a tonne by 2016. That should mitigate the impact of lower potash prices on the company’s bottom line.

Of course, investors may never get to see the golden days of 2009 when potash demanded more than US$800 per tonne. However, the potash industry has matured and consolidated since, which should put a cap on stretched valuations and expectations going forward. Its leadership position, its focus on cost control, and its flexibility of operations should help Potash Corp. ride out a storm.

Potash Corp.’s profits may take a hit if nutrient prices head lower, but it’s unlikely to hurt shareholder returns, at least in terms of the generous dividends that the company doles out. With capital expenditures expected to decline in the near future as major projects near completion, Potash Corp. will have greater cash flows at its disposal to return to shareholders. That’s a huge positive for investors, especially when the market looks shaky.

With the stock now trading at a P/E near five-year lows, much of the pessimism appears to have been factored into its share price. More importantly, the stock’s recent fall has taken its dividend yield to an all-time high of 7%, which should give even risk-averse investors confidence in the company. At today’s price, Potash Corp. presents an opportunity for both value and dividend investors.

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