



Why Agrium Inc. Investors Should Remain Cautious This Week

Description

Investors in **Agrium Inc.** (TSX:AGU)(NYSE:AGU) should brace themselves for a volatile week as the agricultural company prepares to release its third-quarter earnings before the market opens on November 5.

Peer **Potash Corporation of Saskatchewan Inc.'s** (TSX:POT)(NYSE:POT) surprisingly weak Q3 numbers reported last week has made the market wary—Potash not only missed analysts' estimates, but also lowered its full-year guidance, signaling greater pain ahead for fertilizer companies.

While Agrium has hugely [outperformed](#) Potash this year, it isn't immune to the macro challenges that Potash outlined in its Q3 report. There are high chances of Agrium reporting weak numbers and downgrading its outlook this week. Here's why.

Potash's numbers indicate trouble for Agrium

During the second quarter, Agrium lowered its full-year guidance despite strong growth in its quarterly profit. It projected 2015 earnings per share to range between US\$7 and US\$7.50, down from its previous EPS guidance range of US\$7-8.25. The company blamed weak potash and phosphate prices and the impact of lower crop prices on demand for its retail segment products for the weak outlook.

Unfortunately, Potash's Q3 numbers confirm Agrium's fears. Potash's selling prices for its namesake nutrient were nearly 11% lower year over year. Worse yet, Potash realized 10% lower price for nitrogen, which is also Agrium's primary nutrient.

Simply put, investors shouldn't expect much from Agrium this week. As wholesale (which is primarily fertilizers) is also its most profitable segment, low nutrient prices will likely hit Agrium's bottom line.

Why lower guidance isn't unlikely

Things don't look too good with Agrium's retail side of business either. For instance, seed giant **Monsanto** reported 9% drop in its seeds and genomics sales for the last quarter, with corn seed sales continuing to fall. With Canada's grain crop projected to breach its five-year average this year,

Agrium's retail gross profit could suffer.

Combined, the challenges could mean that Agrium's Q3 earnings will fall short of consensus estimates of US\$7 per share, even compelling the company to further reduce its full-year guidance.

The key point to note

Investors should look beyond the numbers and focus on how Agrium plans to deal with the difficult times. Any plans to restructure in the form of plant shutdowns or layoffs could indicate tougher times ahead. Potash, for instance, is cutting back production in the fourth quarter.

More importantly, keep an eye on Agrium's cash flows. Higher dividends in recent times have been a major attraction for Agrium investors. But whether or not the company's aggressive dividend policy (its quarterly dividend has grown 75% in two years) is sustainable will largely depend on how much cash it can generate even in challenging business conditions.

You must know that Agrium is currently free cash flow negative. So, any further dividend growth could spell danger until its cash flow improve. How Agrium plans to improve cash flow should be among the key things to watch for in its upcoming earnings report.

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1. Investing

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