



Potash Corporation of Saskatchewan Inc. Investors Could Be in Trouble if This Rumour Comes True

Description

Less than two months since **Potash Corporation of Saskatchewan Inc.** (TSX:POT)(NYSE:POT) withdrew its bid for German potash player K+S, the rumour mill says the fertilizer giant is at it again.

According to *Reuters*, German investor newsletter *Platow* recently reported that Potash is preparing to come up with “a fresh takeover approach” for K+S early next year. Potash chased K+S for more than three months before pulling out a couple of months ago, citing “a lack of engagement by K+S management” as the key reason.

While it’s only a rumour for now, what if it comes true? After all, Potash was eager to buy out the German company, so a renewed interest would not be surprising. The problem is that it may not help investors if Potash acquires K+S at this point in time.

Why Potash could bid for K+S again

K+S believed Potash wanted to acquire it primarily to gain control over its greenfield potash project, Legacy, which is expected to go online next year. As Legacy will commence production at a time when the potash market is facing a supply glut, K+S contended that Potash aimed to curtail production at the mine to support nutrient prices.

Unfortunately, the potash market has deteriorated further in the past couple of months, forcing major producers like Potash and **Mosaic** to cut down production. Potash is closing down its Penobscis mine at New Brunswick ahead of schedule and is temporarily shutting down three plants this month, and Mosaic is planning to run its potash plants at only 70% capacity this quarter.

Given the backdrop, it shouldn’t be surprising if Potash takes bolder steps to improve the demand-supply situation. While Potash insisted it never intended to close down K+S’s mines or projects, control over the plants would still give it leeway to adjust production volumes and reduce supply in the industry.

Why investors need to worry

While the idea of being able to balance demand and supply through a larger market share sounds good, the implications of Potash acquiring K+S go beyond that.

Investors may recall that Potash was willing to shell out a whopping \$8.7 billion for K+S, which the latter found inadequate. So Potash may have to raise its bid, which could mean a huge cash outflow amid challenging business conditions.

With potash prices unlikely to hit the highs of 2009 (which were nearly triple that of current spot price) and recovery expected to be slow, Potash could end up overpaying for a high-cost, low-cash flow-generating company at a time when its margins are already under pressure.

Not the right time

Acquiring K+S could give Potash control over 30% of the global potash supply, but this may not be the right time for this acquisition. We've seen how mining-equipment manufacturers and gold miners splurged on acquisitions during lull times, expecting a strong pay back in anticipation of a recovery in the mining industry. Years later the recovery is still nowhere in sight, leaving those companies cash-strapped.

Investors can only hope Potash doesn't find itself in a similar situation, given how sensitive the demand for its namesake nutrient is to volatile agricultural commodities.

CATEGORY

1. Investing

POST TAG

1. Editor's Choice

Category

1. Investing

Tags

1. Editor's Choice

Date

2025/09/12

Date Created

2015/12/02

Author

nehams

default watermark