Why Agrium Inc.'s Profits Jumped 24% While Potash Corporation of Saskatchewan Inc.'s Slumped 17% Last Year

Description

The earnings season is a great time to dive into a company's financials and find out its standing in the industry. Consider **Agrium Inc.** (TSX:AGU)(NYSE:AGU) for instance. The fertilizer player delivered solid numbers earlier this week at a time when rivals are struggling to cope with the changing dynamics of the industry.

Agrium's fourth-quarter and full-year earnings jumped sharply in contrast to competitor **Potash Corporation of Saskatchewan Inc.'s** (TSX:POT)(NYSE:POT) declining income.

In 2015 Agrium's gross profit climbed 9% and net income (from continuing operations) surged 24% despite an 8% drop in sales. Comparatively, Potash Corporation's gross profit and net income slipped 14% and 17%, respectively, last year.

So what's giving Agrium the lead? It's a tale of two factors: the company's product mix and a two-fold approach to challenges.

Nitrogen vs potash

While Potash Corporation is a pure-fertilizer play, Agrium operates two business segments: wholesale (fertilizers) and retail (seeds and crop protection products). Wholesale is a high-margin business and the more profitable of the two.

Within wholesale, Agrium's primary nutrient is nitrogen, unlike Potash Corporation, which depends largely on its namesake nutrient for sales. So while a slump in the demand and prices of potash hit the latter hard, Agrium's nitrogen gross profit surged 65% in Q4 thanks to lower prices of key input, natural gas, and higher production volumes. That drove up the company's wholesale profits significantly.

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Source: Company earnings call presentation
Agrium's Q4 2015 Wholesale gross profit break up. Source: Company earnings call presentation

Meanwhile, Agrium's share in Canpotex–the export association between Potash Corporation, **Mosaic**, and Agrium that handles potash exports to markets outside the U.S. and Canada–increased three percentage points to 10.3% Q4 onward thanks to the expansion of its Vanscoy potash mine. That boosted its potash sales and profits.

Given the prevailing weak conditions of the global potash markets, Agrium's focus on nitrogen should continue to help it grow its profits going forward.

A smart strategy

While every fertilizer company is curbing expenditures during these difficult times, Agrium is doing a commendable job. It reduced its selling, general, and administrative expenses by nearly 7% last year. Comparatively, Potash Corporation's SGA expenses declined only about 2% in 2015.

In short, Agrium is using a two-pronged approach to turn challenges into opportunities: it's expanding low-cost facilities while cutting unnecessary costs. This strategy is not only helping Agrium weather the storm, but is also giving it an edge over rivals.

Will Agrium continue to reap profits in 2016?

While both companies have a muted outlook for 2016 as macro headwinds remain strong, Agrium's guidance is less cautious. Its earnings-per-share range calls for a drop of 21% to a *rise* of 3% over 2015. Potash Corporation, on the other hand, expects a 21-41% drop in its EPS this year. That could also mean more safety for dividend investors as Agrium may not have to resort to a dividend cut, unlike Potash Corporation, which slashed its quarterly dividend by 34% last month.

Given the backdrop, I strongly believe that Agrium has the potential to be the strongest fertilizer stock in 2016. Keep an eye on this one.

CATEGORY

1. Investing

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