# Read This Before Buying Potash Corporation of Saskatchewan Inc. on the Dip

## Description

Thanks to another disastrous set of quarterly numbers, **Potash Corporation of Saskatchewan Inc.** (TSX:POT)(NYSE:POT) has lost nearly 4% in two days' time. With that, the stock is now down 8% year to date and 45% in one year.



That hugely underperforms peer **Agrium**, which is down only about 15% in the past year, which raises a vital question: With Potash Corp. stock almost kissing its 52-week lows, is it time to buy? While I highlighted the fundamental reasons to avoid the stock in a recent article, I'll answer that based on valuation here.

**Wow, that's cheap!**

Based on its current valuation, Potash Corp. is very cheap. The stock is trading at under 12 times trailing earnings, which is a significant discount to industry average P/E of 20 as well as Potash Corp.'s own five-year average P/E of 17. Likewise, the stock is cheap based on price/book and price/cash flow ratios.

But let's dig a little deeper to find out Potash Corp.'s worth based on enterprise value. Why enterprise value? Because it values a firm as if it were about to be bought today and is thus a more accurate measure than simple market capitalization that we use to calculate the P/E ratio.

**Oh wait, it isn't!**

Potash Corp.'s market cap currently stands at US$14.7 billion. I'm taking the figure in U.S. dollar since the company reports in that currency. Potash Corp. currently shoulders net debt worth roughly US$4.9 billion and holds cash and equivalents worth US$91 million. All together, that works out to an enterprise value, or debt-adjusted market capitalization in simpler terms, of around US$18.7 billion.

Now if we divide Potash Corp.'s last 12-month profits of US$1.27 with the adjusted market cap, we get a P/E of 14.7 times. Potash Corp. suddenly doesn't seem that cheap anymore, does it?

Also, its price-to-free cash flow (enterprise value to FCF) now comes up to nearly 17 times based on the company's FCF of US$1.1 billion in the last 12 months. Now that's expensive, considering that analysts expect Potash Corp.'s earnings to decline nearly 40% this year and roughly 2% over the next five years. Why would you pay 15 or 17 times for a company that may not grow at all in the near future?

**Any respite for income investors?**

If you like Potash Corp. for its dividend, know that it paid out roughly 120% of its free cash flow in dividends last year. That's a red flag, because it isn't sustainable.

With earnings expected to under tremendous pressure given the deteriorating conditions of the fertilizer markets, Potash Corp.'s cash flows could fall. Even if Potash Corp. pays out 100% of its FCF to shareholders, a lower FCF would mean lower dividends, unless the company buys back enough shares to reduce the number it has to pay a dividend on. That's not growth in the true sense. Moreover, even a dividend 6% yield doesn't justify a P/E of 15 times when profits aren't growing.

Long story short, Potash Corp. may appear to be a bargain, but it definitely isn't the best bet out there. There are stocks that can fetch you massive returns, like the one mentioned below.

**CATEGORY**

1. Investing



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