Potash Corporation of Saskatchewan Inc. Shares Are Near 9-Year Lows: Is it Time to Buy?

Description

Warren Buffett was once quoted as saying, “Cash combined with courage in a time of crisis is priceless.” For **Potash Corporation of Saskatchewan Inc.** (TSX:POT)(NYSE:POT) shareholders, there is little doubt the past couple years have been a time of crisis.

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The situation at Potash Corp. is so dire that an investor who bought in March 2007 would have nothing to show for the time period; and shares are down 70% since the 2008 high, and 10% year-to-date.

Recently, the downside in Potash Corp. has been driven by a few factors.

A contract between Canpotex (the potash marketing consortium that Potash Corp. is part of) and China has not yet been set for the year (the contract is usually done before spring), sparking concerns over demand. And the collapse in potash prices has continued, driven by falling crop prices, weakness in key potash currencies, and elevated inventories globally. The fear of more global supply coming online has also been a factor.

What does this mean for Potash Corp. shares? Many of these concerns are now being alleviated, which means that while a rally in Potash Corp. is uncertain, there is a good chance the bottom is in.

Canpotex is about to finalize a contract with China

Potash contracts with China (the world’s largest buyer) are usually set early in the year, and the major delay this year has been bad news for markets. The prices set in contracts with China set the global benchmark for pricing, and the main fear was that without major producers dealing with China on a contract basis, the market would move a much more competitive spot prices.

Producers banding together and setting contracts with China has led to higher prices; the end of the system would be bad news for potash prices.

The lack of China contracts also had the effect of stalling the entire market. Since the prices set by contracts with China serve as the global benchmark, the absence of contracts left other buyers on the sidelines. This meant that for the first half of 2016 potash deliveries were very slim due to a lack of shipments to China as well as India.

While the delay has certainly been negative, recent developments are overwhelmingly bullish. Firstly, major Belarusian producer BPC settled a Chinese contract at a better-than-expected potash price of $219/mt. Canpotex will likely settle soon at the same price, and this means volumes will move into China for the second half of the year.

This also means that there is likely to be a big jump in demand coming soon. In 2013 the potash market was shocked when Uralkali and Belaruskali disbanded their marketing cartel, which sent prices plunging. As a result, buyers stayed out of the market due to uncertainty (drawing down inventories instead), and the result was that 2014 saw a huge explosion of demand as buyers jumped back into the market.

Potash Corp. thinks the delay in the China contract will result in a 5-15% boost in demand as it has in other years when the contract was delayed.

There has been a supply response to low prices

With demand being bunched into the second half of 2016 and into 2017, the demand outlook for potash is strong. Global demand is likely to grow from 60 million tonnes this year to between 61 and 63 million next year.

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Supply has also been coming offline thanks to low potash prices. There have been six million tonnes of potash curtailments announced (1.8 million tonnes from Potash Corp.), which should bring total 2016 potash supply to 58 million tonnes. With demand of 60 million tonnes, this means that in 2016 the market is actually short two million tonnes.

While this doesn’t mean Potash Corp. is set to rally, it does mean investors can likely enter now without worry of much more downside.

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