



3 Reasons Potash Corporation of Saskatchewan Inc. Shares Have Likely Bottomed

Description

Famed trader Paul Tudor Jones once said, “the best money is made at market turns,” and while this may be true, the challenge comes in identifying these points. Identifying the precise end of a stock’s bear market is likely impossible, but it is certainly possible to identify prices where the potential upside greatly exceeds the downside. For **Potash Corporation of Saskatchewan Inc.** (TSX:POT)(NYSE:POT) shareholders, current prices in the low \$20 range may be this point.

Potash Corp. has endured a decline in realized potash prices from \$424 per tonne in 2012 to \$154 per tonne in the latest quarter. These declines were driven by the break-up of the joint marketing cartel between Uralkali and Belaruskali in 2013, which led to both producers pursuing a market share-based strategy. This development coincided with a slew of new supply as Potash Corp., **Agrium**, **Mosaic**, and **K + S** all commenced on multi-billion-dollar potash capacity expansions.

At the same time, record crop yields (which lowered crop prices) and extreme weakness in key potash purchasing currencies weighed on demand from major potash buyers (such as Brazil) and bolstered the cash flows of potash producers (like Russia).

These key factors, which drove down prices, are now almost all showing signs of improving, and the result should be limited downside.

The annual Chinese contract is set to be settled soon

Much of 2016’s weakness can be attributed to the fact that as of June, none of the major global producers set a contract with the largest global consumer—China. The lack of a Chinese contract worried markets because it could’ve meant the market was moving towards a much more competitive spot market rather than producers entering into longer-term, higher-priced contracts.

The lack of a Chinese contract also kept many buyers on the sidelines because the China price is a key benchmark. Fortunately, Belarus (a major potash producer) recently signed a Chinese contract at prices of \$219 per tonne (better than expected), and Israeli producer ICL also signed a contract.

Canpotex (Potash Corp.'s marketing cartel) should be up next. This will provide stability to the market and move volumes into China.

There has been a global supply response to lower prices

Low potash prices are broadly working to take high-cost production offline. Since 2014 six million tonnes of potash capacity have come offline, almost all of which have come offline permanently. Potash Corp. itself just closed its New Brunswick mine, and Mosaic just shut down its Colonsay mine. Six North American mines in total have closed—all of which were on the expensive end of the cost curve.

As a result of this, with potash demand coming in at 60 million tonnes (expected) for 2016, expected supply of 58 million tonnes will actually leave a supply deficit, which is supportive of prices. Moreover, 2016 operating capacity is expected to be about 65 million tonnes, according to Potash Corp., and going into 2017 Potash Corp. sees this rising by only one million tonnes, despite the fact that demand is expected to grow by one to three million tonnes.

The demand outlook is improving

Global demand growth is expected to still be strong. As previously mentioned, 2016 demand is expected to be between 59 and 60 million tonnes, growing to 61-63 in 2017 (Potash Corp. sees 62.5).

The second half of 2016 and 2017 should see "demand bunching" as well. The first half of 2016 saw many buyers on the sidelines, and this means a decline in inventories. Similar to 2013, when buying stopped due to the break-up of the BPC cartel, 2014 saw a massive rebound of demand as buyers looked to re-stock inventories.

Potash Corp. noted that in years with late Chinese contract settlement, demand jumped between 5% and 15% the following year thanks to this phenomenon. On top of this, fertilizer remains very affordable for farmers; fertilizers are 21% more affordable than the average since 2010, according to Mosaic.

At the same time, there is strengthening being observed in key potash currencies such as the Brazilian real. This will only support demand, giving Brazilians more purchasing power to acquire potash that is priced in U.S. dollars. A 25% surge this year reverses a key factor that has weighed on potash prices.

CATEGORY

1. Investing

POST TAG

1. Editor's Choice

Category

1. Investing

Tags

1. Editor's Choice

Date

2025/08/25

Date Created

2016/08/25

Author

amancini

default watermark

default watermark