



Are Potash Corporation of Saskatchewan Inc. and Agrium Inc. About to Merge?

Description

Some interesting rumours are swirling about two agricultural giants.

According to reports, **Potash Corporation of Saskatchewan Inc.** (TSX:POT)(NYSE:POT) and **Agrium Inc.** (TSX:AGU)(NYSE:AGU) are in talks about a merger. Shares of both companies surged on the news, with Potash Corp. shares increasing as much as 10% and Agrium shares up as much as 9%. Both have since been halted because of the volatility.

The market is right to react strongly to this potential deal. Here's why it's a very good idea.

Struggling potash prices

Potash Corp. has been struggling over the last few years as conditions in the potash market went from spectacular to merely good to terrible.

The big issue has been oversupply. Just a handful of producers controlled supply in a tight-knit cartel. This propped prices up nicely. Unfortunately for everyone involved, a couple of Russian producers decided to ignore production quotas and flood the market with potash. This extra supply drove prices down.

These lower prices hit Potash Corp. right in the bottom line. Profits in 2012 were \$2.37 per share and \$2.04 per share in 2013. According to analyst projections, net profit is expected to fall to \$0.98 per share this year and \$1.12 next year.

Agrium hasn't been nearly as affected. This is because the vast majority of its business is in the retail side of things. Potash supplies the raw material, while Agrium sells it to farmers. With farmers just about everywhere in North America flush with cash because of bumper crops and low interest rates, it's been a lot better to be in that part of the supply chain.

The synergies make a lot of sense. By combining the major supplier and retailer of fertilizer, the new combined company would be in the unique position of essentially controlling the North American market. It would also ensure plenty of demand for Potash Corp.'s namesake mineral.

Potential regulatory issues?

It's going to be interesting to see if this proposed merger can pass the scrutiny of regulators—assuming it gets that far, of course. At this point, the two companies are merely in discussions, nothing more.

Although there doesn't seem to be a whole lot of overlap on the surface—Potash Corp. is a producer, while Agrium is the retailer—there's still the chance regulators may balk at one combined entity controlling so much of the input market.

This is certainly a bigger issue in Canada than in the United States. Although I don't think it'll be an issue, it's probably something investors looking to invest in a newly combined Agrium and Potash Corp. should at least be aware of.

Should you invest?

It's silly to invest in rumours. The two companies haven't even reported publicly that negotiations are going on yet. At a minimum, investors should wait until the companies report that talks are going on.

There are certainly a lot of advantages of the two companies combining, however. There's a reason why shares of each company surged just on rumours. If the two do come together, there's a lot to like.

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