What the Agrium Inc./Potash Corporation of Saskatchewan Inc. Merger Means for Investors

Description

This past week, representatives of both **Agrium Inc.** (TSX:AGU)(NYSE:AGU) and **Potash Corporation of Saskatchewan Inc.** (TSX:POT)(NYSE:POT) announced a proposed "merger of equals." The deal will result in a combined company that would not only be the largest crop-nutrient supplier in the world, but would also have a market cap of nearly $35 billion and operations in nearly 20 countries.

Here's a look what this merger could mean for both of the involved companies as well as investors.

What this means for Potash Corp.

Potash Corp. may be the larger company going into the deal, but whether or not Potash Corp. is entering as the better investment is up for debate. Post-merger, Potash Corp. will account for 52% of the new company; current shareholders will get 0.4 shares for every existing Potash Corp. share.

Potash Corp. is already the world's biggest crop-nutrient company, but fertilizer prices have been anything but profitable over the past few years. Potash prices in particular have fallen by over 80% in the past eight years with the average price per tonne coming in at approximately US$150 this past quarter–a significant drop from the US$275 per tonne potash was fetching on the market just a year ago. Back in 2008, that price was even higher at US$800 per tonne.

With potash prices remaining relatively weak and change in price looming on the horizon, Potash Corp. needs this deal. The company could arguably pursue a different approach akin to how gold producers shuttered more expensive facilities and focused on improvements during the precious metals price drop, but the Agrium deal may be the best chance for Potash Corp. in the foreseeable future.

Potash shareholders who have already seen their dividend slashed twice in the past year could see an increased dividend as part of the deal at the expense of a much healthier Agrium.

What this means for Agrium

There are some doubts surrounding the deal from the perspective of Agrium, which, in fairness, are well founded. As part of the deal, Agrium will get 48% of the new company, and existing Agrium shareholders will be granted 2.23 common shares of the new company for every existing Agrium share.

Agrium is already the largest global distributor of crop supplies in North America, and, unlike Potash Corp., already has strong results to back up the company and a massive network of over 1,500 retail and wholesale locations in the U.S. and Canada. Agrium also locations in South America and Australia, where services to support over 50 different crops are made available.

In short, Agrium’s business is strong, especially since the strongest part of the year from an earnings perspective is about to begin; crops will come in, and farmers will purchase supplies for the next year.

This merger may seem risky for Agrium shareholders, who have long been represented as the safer investment of the two companies, but executives from both companies have stated that the long-term interest of both companies is in this merger.

Benefits of the merger

Two points are constantly brought up regarding this merger: the potential cost savings that both companies could realize, and the strategic shift that will set up the new company for years of growth.

On the cost front, some of the claims being made state the potential of $500 million in savings. Upwards of $150 million is likely to surface from integrating Agrium’s retail network with Potash Corp.’s wholesale operations. There is some overlap between the two companies’ retail and production footprints, particularly in the corn belt, where these savings could be substantial.

Additional savings of up to $200 million could arise from both overhead reduction costs as well as procurement and capital efficiencies.

The deal will likely attract scrutiny from a number of regulatory bodies as well as shareholders from both companies, and it could take some time before being finalized.

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Date
2025/07/30
Date Created
2016/09/17
Author
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