Making Sense of the Agrium Inc./Potash Corporation of Saskatchewan Inc. Merger

Description

When times are rough, as they have been for potash companies for quite a while, a big merger can be just what is needed to reduce costs, increase margins, and ultimately make all investors richer. But not all mergers are created equal. And the road to riches is paved with good intentions.

All of that aside, the proposed merger between **Agrium Inc.** (TSX:AGU)(NYSE:AGU) and **Potash Corporation of Saskatchewan Inc.** (TSX:POT)(NYSE:POT) appears to have all the right points in place that should make this deal a success for investors of both companies. And there are multiple reasons for that.

By merging, the combined company will be able to achieve approximately $500 million in operating synergies *without* any market condition improvement.

Here's how…

First, by combining the two operations, the company will become the second-largest provider of nitrogen in North America. It will also become one of the largest providers of potash and phosphate, giving it more control of how much of its supply to sell at any given point.

Purchasing costs are estimated to be reduced by ~4% across the two companies, which will provide US$100 million in value. It'll look to save US$25 million by eliminating redundant warehouses with US$20 million coming from Agrium's leased warehouses. But the biggest savings is in selling, general, and administrative expenses. It hopes to see US$125 million in synergies by eliminating duplicate public company costs, optimizing HQ functions, and reducing discretionary, non-personnel G&A spending by US$60 million.

Clearly, there is the potential for a lot of cost savings.

But what I am particularly bullish on is how Potash can benefit from Agrium's retail business. Presently, Potash is only in the wholesale business; however, once it merges with Agrium, it'll be able to sell its products in Agrium stores. And the company sees that as a big gain as well. So far in 2016, it has acquired 65 additional retail locations and has done US$500 million in sales. By pushing Potash products through, it expects to see its 2020 retail EBITDA anywhere between US$1.3 and US$1.4 billion.

What's nice for both companies is that this merger will help diversify where EBITDA comes from. Presently, Agrium generates 53% from retail, 9% from potash, 6% from phosphate, and 32% from nitrogen. Potash generates 38% from nitrogen, 19% from phosphate, and 43% from potash. The two companies will generate 28% from retail, 25% from potash, 35% from nitrogen, and 12% from phosphate.

The terms of the deal are pretty straight forward. Once the merger goes through, Potash shareholders will own 52% of the new company, receiving 0.4 shares for every Potash share, and Agrium shareholders will own 48% of the new company, receiving 2.23 shares in the new company for every Agrium share. The goal is to be done by mid-2017.

But is it a good deal?

I think so. If the combined company can achieve those sorts of cost savings, it will be in a much better position to ride out low potash prices. Further, the additional balance sheet resources will enable the new company to expand more aggressively in retail, which generates good margins. All in all, I think investors should be excited about this opportunity.

CATEGORY

1. Investing
2. Metals and Mining Stocks

Category

1. Investing
2. Metals and Mining Stocks

Date
2025/07/21
Date Created
2016/10/19
Author
jaycodon