



Should You Exit Potash Corporation of Saskatchewan Inc. Before 2017?

Description

The recent rally in **Potash Corporation of Saskatchewan Inc.** (TSX:POT)(NYSE:POT) stock has come as an early Christmas gift for investors. The stock looked set to end 2016 on a weak note until about two months ago, when it dramatically reversed course to gain almost 15%.

End markets haven't really improved much, Potash Corp. has slashed its dividend, and the stock is already trading steep at 33 times trailing earnings. Comparatively, **Agrium Inc.** (TSX:AGU)(NYSE:AGU) is still trading under 20 times trailing earnings, despite rallying as much as Potash Corp. in the past quarter. So would you be better off selling Potash Corp. stock as you head into the new year?

2016: A year of tumbling profits and dividend cuts

This year was among the most challenging years for Potash Corp. As demand and prices of fertilizers deteriorated, the company's sales and net income tumbled almost 25% and 62%, respectively, in the trailing 12 months.

Potash Corp.'s cash flows crashed, and it soon realized maintaining the dividend would be impossible as it was already paying out 100% of its profits in dividends. Potash Corp. slashed its dividends not once, but twice during the year—first by 34% and then by a whopping 60%.

In sharp contrast, Agrium maintained its dividend throughout the year, despite operating in similar challenging environment. Not surprisingly, Potash Corp. stock lost favour with investors.

The surprise U-turn in September

Just when Potash Corp. investors had given up hopes of a recovery, the company caught them off-guard by announcing its intention to combine with Agrium in a "merger of equals." While the merger is still awaiting regulatory approval, the [terms clearly favour](#) Potash Corp., which is why Potash Corp. stock gained has some ground.

For starters, the share exchange ratio implies a zero premium for Agrium shareholders. Second, and

more importantly, Agrium's retail arm—which is a high-margin and relatively resilient business that deals in seeds and crop nutrient and protection products—will reduce Potash Corp.'s exposure to the volatile fertilizer markets. That should mean more stable earnings for Potash Corp. going forward.

Potash Corp. is a risky stock

Don't get me wrong; I'm not writing off Potash Corp. because fertilizers are essential to boost crop productivity as the global population rises and arable land shrinks. Also, Potash Corp. is one of the top fertilizer producers in the world.

My only concern is that the stock appears to have gotten ahead of itself. The merger is good news, but there's no clarity about the financial benefits yet, and much of the optimism appears to have been already baked into Potash Corp.'s stock after its recent rally. To top that, potash prices may not recover much in 2017 if China and India delay contracts, and that could keep a lid on the company's earnings. Keep that in mind before betting on Potash Corp. for 2017.

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