Can Potash Corporation of Saskatchewan Inc. Get its Head out of the Dirt?

Description

Potash Corporation of Saskatchewan Inc. (TSX:POT)(NYSE:POT) has been a tough stock to hold over the last few years. Many contrarian investors have tried to catch a bottom but have not had much luck. The stock rallied by as much as 29% from the August 2016 trough to the January 2017 peak, but it has since started to give up these gains because the medium-term outlook for potash still looks bleak.

The demand for potash in China and India, two of the largest markets for the commodity, isn't looking like it will increase by a meaningful amount anytime soon. There's a real chance that Potash Corp. could give up all the gains from the recent rally as it heads back to 52-week lows.

Potash Corp.'s Q4 2016 numbers were extremely underwhelming. The earnings per share were at a minuscule US$0.07 for the quarter, which was much less than what the company had during the same period last year.

Demand looks like it could be near a bottom, but when will the rebound be? Many contrarian investors are loading up on Potash Corp. stock as they believe potash prices will inevitably rebound, and this will give them huge gains over a short period of time. Potash is a necessary commodity that will be around for many decades down the road, but the problem is, the much-anticipated rebound may take a lot longer than expected.

The USDA (United States Department of Agriculture) estimates that crop prices will remain low, and farm incomes are expected to decline even further from here. Lower farmer income means less potash demand, and this is a trend that is very unlikely to reverse over the next year.

What about the valuation?

The stock currently trades at a 44.44 price-to-earnings multiple and has a 2.28% dividend yield. The dividend was slashed a few times, but I don't think another cut is in the cards this year as the payout is likely to remain static.

The price-to-book multiple is ridiculously cheap at 1.8, which is much lower than the company's five-year historical average multiple of 3.2. I do believe there's a considerable margin of safety at the $22 level, and long-term investors with a time horizon of 10 years or more will get rewarded for their patience. But since there are no real medium-term catalysts, the rebound could be many years down the road, and you could get stuck with sub-par returns over the next year or two.

Sure, the company is cheap, but that doesn’t mean you should buy it. If you really want to own this stock because of its cheapness, then make sure you’re in it for the super long term, and don’t be surprised if the stock doesn’t go anywhere in a year or two.

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