



Will Trump Milk This 1 Company for Everything it's Got?

Description

In the ever-evolving drama surrounding NAFTA and President Trump's threats of renegotiating the trade pact, the Canadian dairy industry has taken quite a few hits on the chin of late. Canada's largest dairy producer **Saputo Inc.** ([TSX:SAP](#)) has been the topic of discussion by many analysts and investors who are considering what the impact of any sort of retaliatory measures would have on Canadian producers.

With a market capitalization of \$17 billion and global market share rivaling that of some of the largest dairy companies in the world, Saputo is a giant by any standard. Currently the second-largest dairy producer in the United States with approximately one-third of its revenue coming from south of the border, Saputo's fate is inexorably tied to the U.S. market.

Saputo has operations around the world, and while the company has a strong import/export business as well, the majority of the dairy products the company sells in the U.S. market are also produced in the U.S. market, meaning import tariffs or duties on the products it produces in Canada would have little effect for the dairy conglomerate.

What is potentially worrisome for Saputo, however, would be a negotiated change to Canada's supply management system, which has put 72% of the country's milk production in the hands of Saputo, **Agropur Cooperative**, and **Kraft Canada**.

A change in the supply management system would, in theory, reduce the price Canadians pay for their dairy (a big positive for all the lactose-consuming Canadians out there).

This implies, however, that the price dairy producers are able to charge for their goods would be only regulated by the market price, meaning profitability in the Canadian dairy industry would be vastly reduced. With Canada representing a significant portion of Saputo's sales, downward pressure on margins means investors looking to do a discounted free cash flow model for Saputo's future free cash flow will be factoring in lower numbers.

Bottom line

The fate of Canada's supply management system happens to be uniquely tied to an oligopoly of three companies with Saputo being the largest and the only publicly traded name of the bunch. The results of NAFTA negotiations between Canada and the United States in the coming months will be something that markets will be watching closely. Investors should definitely pay attention to the rhetoric and discussion surrounding this topic if considering taking a position or adding to a position in Saputo.

Stay Foolish, my friends.

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Author

chrismacdonald

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