



Which 2 Canadian Blue-Chip Companies Offer +15% Compounded Returns?

Description

Five years ago, if you'd asked a room full of financial experts what would be the one stock they would recommend to clients for a long-term buy-and-hold investment, chances are that **Potash Corporation of Saskatchewan Inc.** (TSX:POT)(NYSE:POT) and **Cameco Corp.** ([TSX:CCO](#))([NYSE:CCJ](#)) would have come up more than a couple of times and may even have been the consensus picks among the group.

Potash and Cameco have long been heralded as blue-chip investments by the investment community at least partially owing to the outlook for the industries they operate in. Potash, a manufacturer of fertilizers, is positioned to benefit from a growing population in combination with a finite and diminishing supply of arable land. Cameco is pointed to as a viable source of clean energy by way of its uranium deposits used to power nuclear power facilities.

Beyond a favourable industry outlook, both Potash and Cameco are as seen as blue chips because within their industries, they own world-class assets. Potash's Saskatchewan mines and Cameco's MacArthur River and Cigar Lake uranium deposits are estimated to have several decades of useful life remaining; further to this, they are among the most cost-efficient operations in their respective markets.

However, a combination of low commodity prices and other external market factors have raised all of this into question of late. Commodity behemoths such as **BHP Billiton Limited** and **Vale SA** are planning big moves into the potash market, and Cameco is still reeling from the after-effects of the Japanese Fukushima disaster.

Potash's sales have fallen \$3.6 billion, or 45%, since 2012, and net profits are 84% lower as a result. Cameco, meanwhile, has seen sales decline in three of the last five years and ended 2016 with a \$62 million net loss.

Potash has been forced to cut its dividend on two separate occasions over the past 18 months. While Cameco has not cut its dividend, it also has not increased the distribution since 2011 and now has a payout ratio in negative territory.

To be truthful, most of the aforementioned factors are completely out of management's control and are

part of the inherent risk of investing in commodity-related stocks. Management of both companies have done their best to weather the storm by cutting costs where appropriate and scaling back on investments and capital expenditures.

Owing to this, both companies have still been able to generate positive free cash flow (FCF), despite a challenging market environment. Potash is expected to produce \$1.22 of FCF per share on earnings of \$0.84 in 2017. Meanwhile, on earnings of \$0.35 per share, Cameco is expected to yield FCF of \$1.27 per share.

Which should you buy?

The outlook for both companies is, for the most part, the same. Short-term risks lay ahead for both, although the long-term stories, which many investors appear to have forgotten, remain intact. Both companies should expect to benefit from ongoing production increases, modest commodity price appreciation, and demographic factors.

Based on current estimates, Cameco appears to offer the better prospective returns for investors. At today's price of \$13, and assuming the company can sustain a pace of 10% earnings growth over the long term, investors should expect to earn a tidy 20% annual compounded return on their investment.

Potash, while not offering quite the same level of returns, is also not a bad investment by most standards. Assuming the same 10% growth rate, Potash would be expected to return 16% compounded annually over a long-term investment horizon.

CATEGORY

1. Dividend Stocks
2. Investing
3. Metals and Mining Stocks

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