



# Fertilizer Industry A View From The Street

**Presentation at 2006 TFI Fertilizer Outlook Conference**

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# Agenda

- How Institutional Investors View Fertilizer Stocks
- Agricultural and Fertilizer Outlook
- Our Investment Opinions
- Q&A



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# Competition for Investor Attention and Funds

- Portfolio managers are constantly judged by their performance relative to benchmarks (e.g. the S&P 500)
  - Portfolio managers often own dozens of stocks
  - Chemicals represent <2% of S&P 500 capitalization
- Most buy-side (mutual fund, pension fund, hedge fund) analysts cover multiple sectors with dozens of stocks
  - Ag Suppliers (Fertilizers, Ag Chem, Machinery)
  - Basic Materials (Chemicals, Paper, Metals)
  - Energy



# The Market Is Forward-Looking

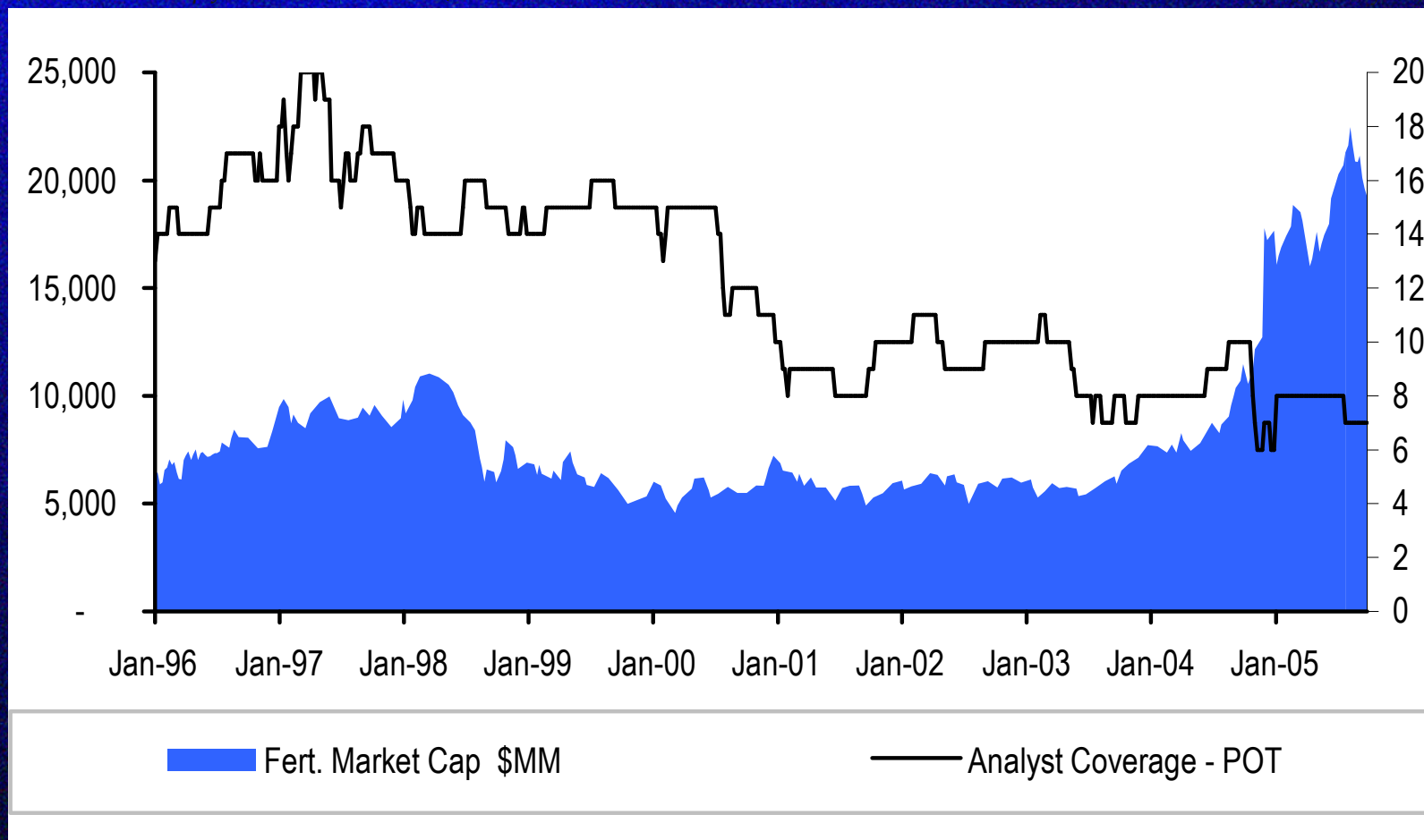
- The market prices-in events before they occur
  - Markets are not always correct and often over-react
- Investors try to buy fertilizer stocks ahead of expected upturn in profitability and sell before the peak actually arrives, eg.
  - Corn condition can be an early indicator of yield, price and subsequent fertilizer demand
  - Anticipated capacity startups or closures have a significant impact on operating rates and fertilizer prices



# Street Coverage Of Fertilizer Sector Well Below Mid-1990s Peak

(total market cap for AGU, POT, IGL/MOS)

(# of analysts)



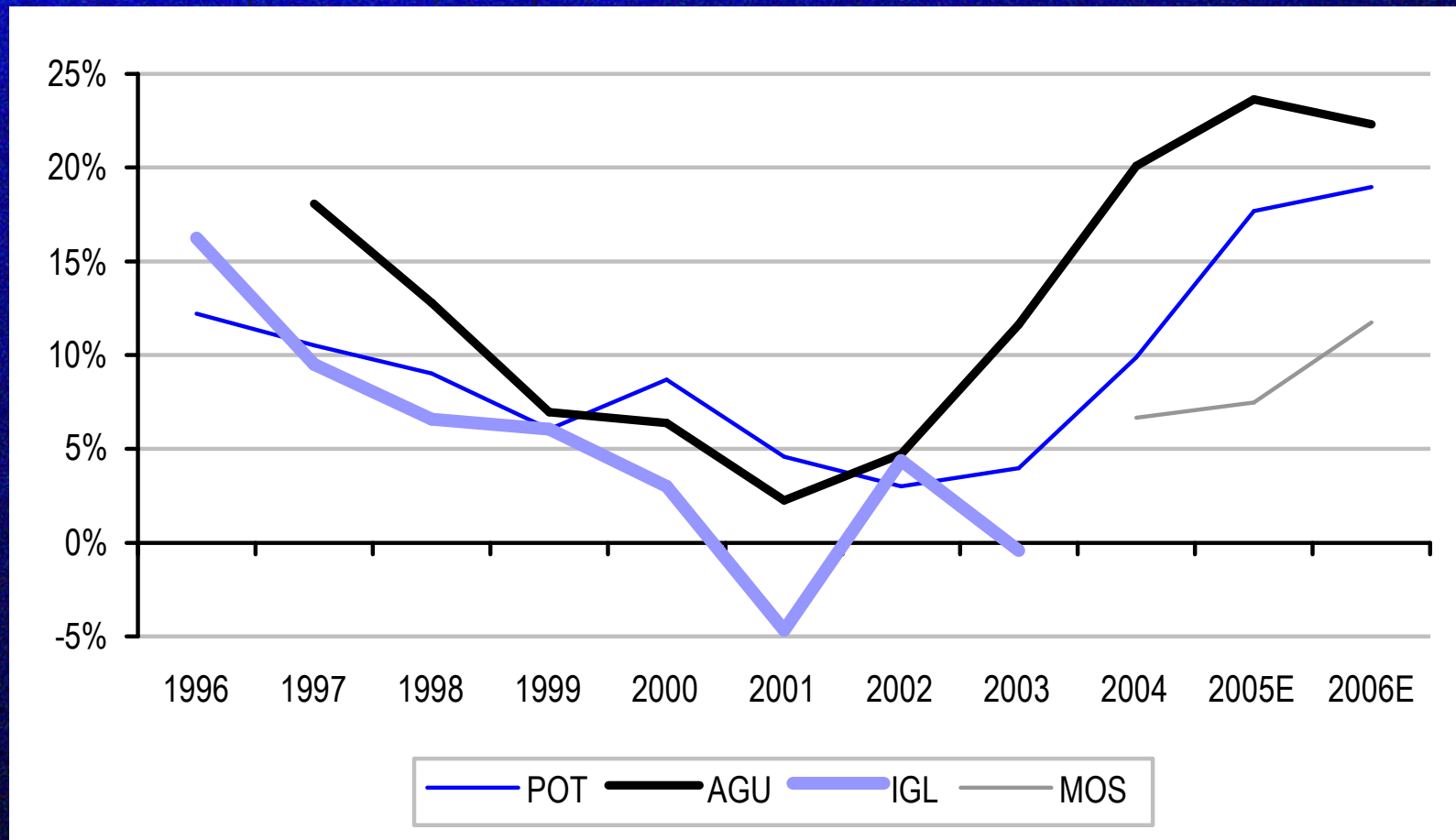
Source: FactSet





# Investors Increasingly Focused On ROC

(return on capital = NOPAT/total capital)

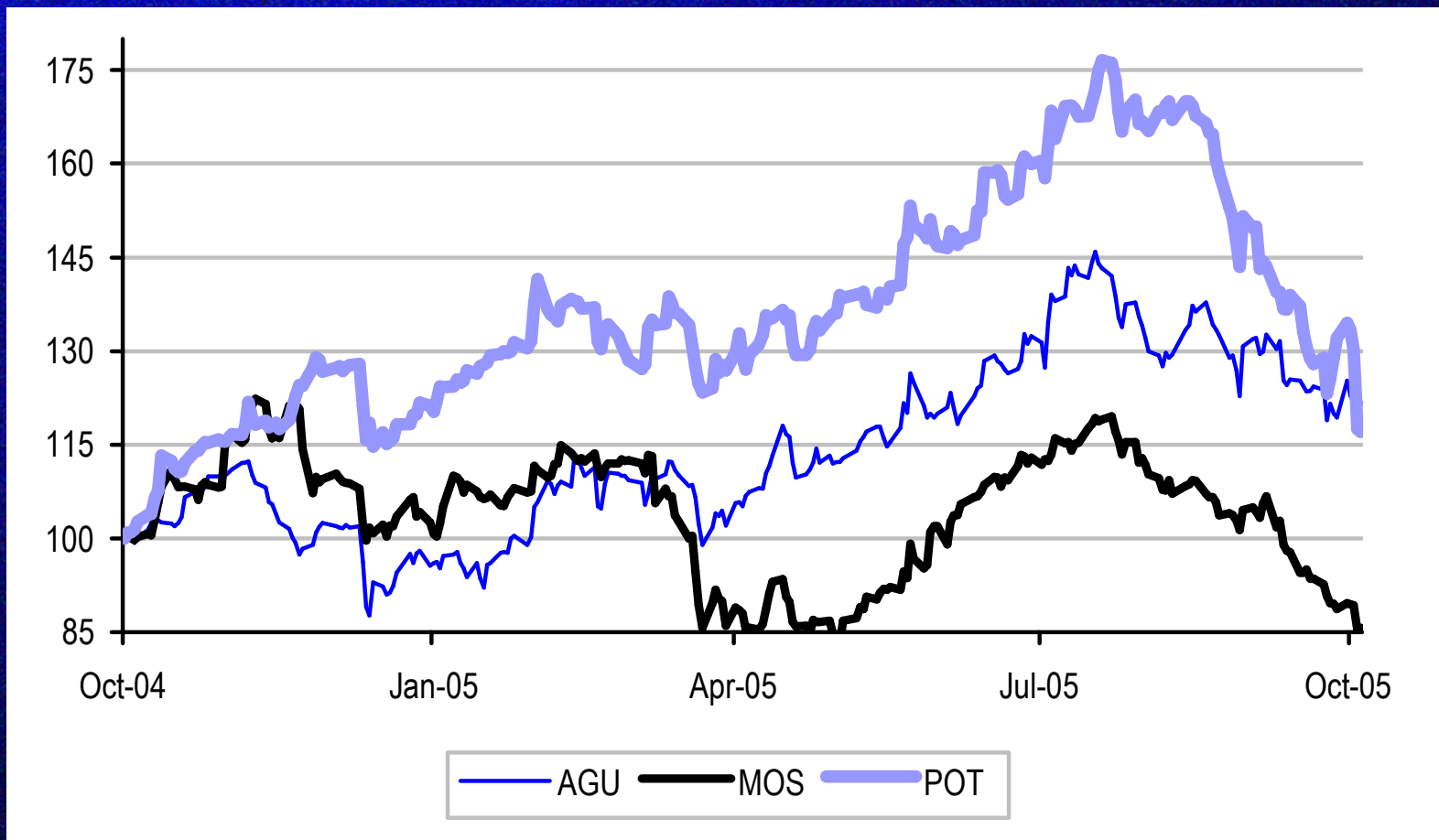


Source: Company reports and ML estimates



# Volatility In Fertilizer Share Prices Creates Opportunities For Active Trading

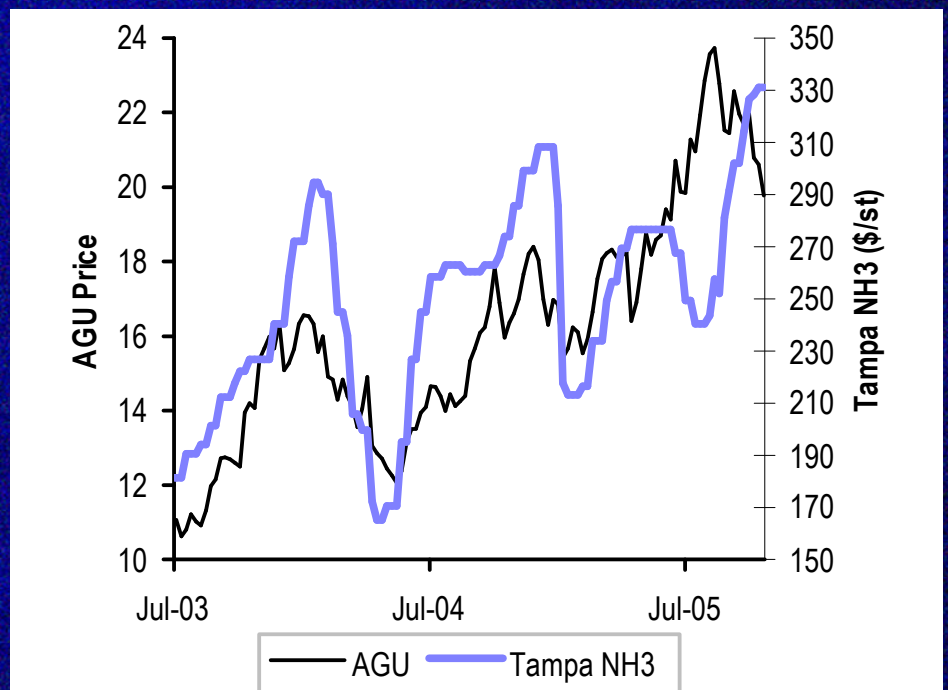
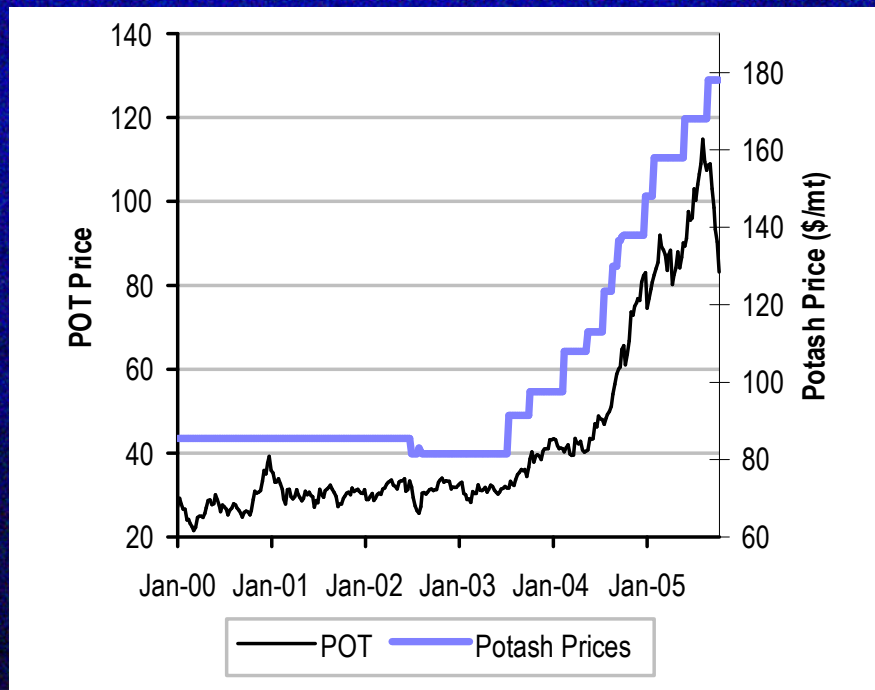
*(normalized stock price)*



Source: Bloomberg



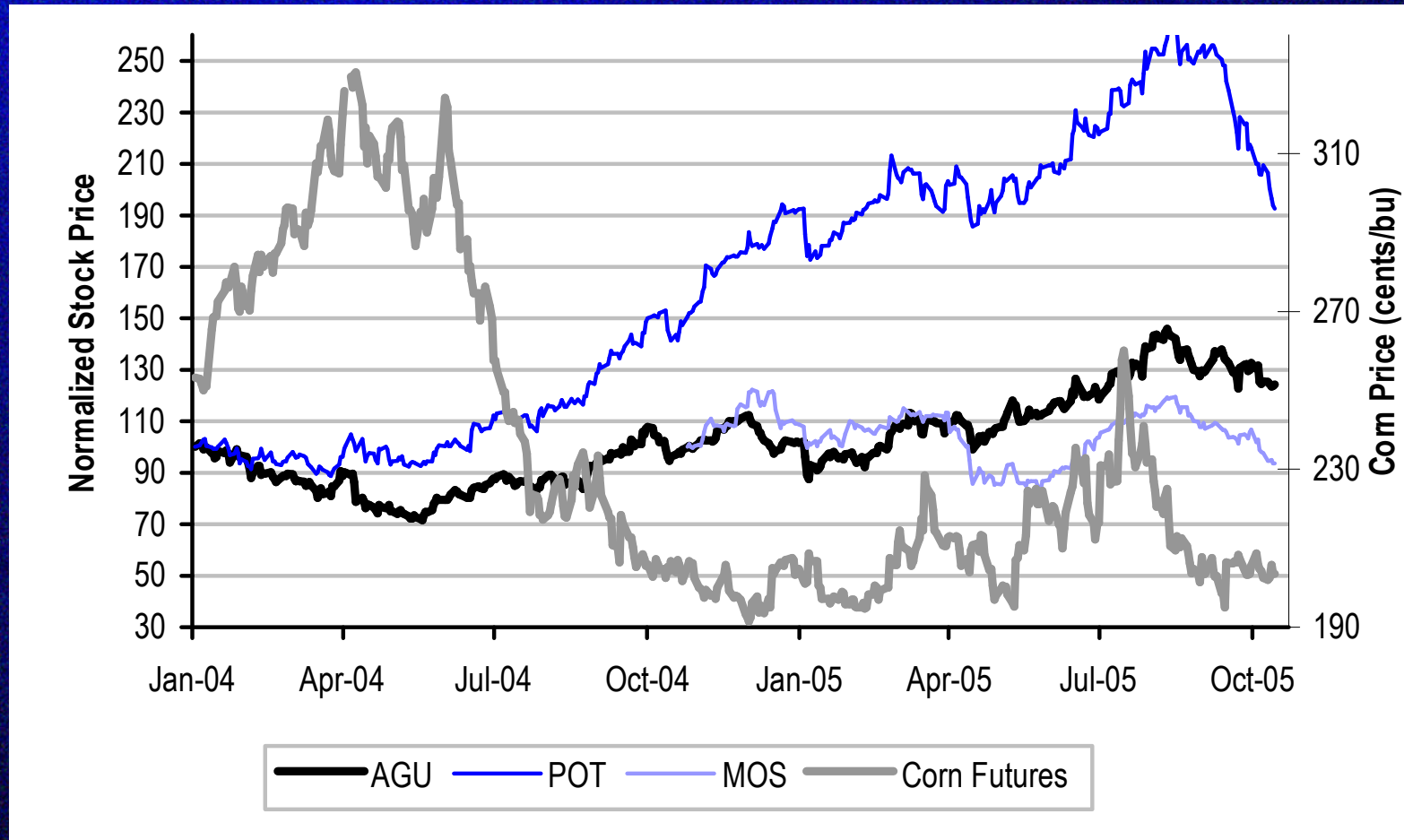
# Fertilizer Stocks Correlate With Fertilizer Prices



Source: Green Markets, Bloomberg



# Fertilizer Stocks Decoupled From Corn Prices In 2004 But Re-coupled In Recent Months



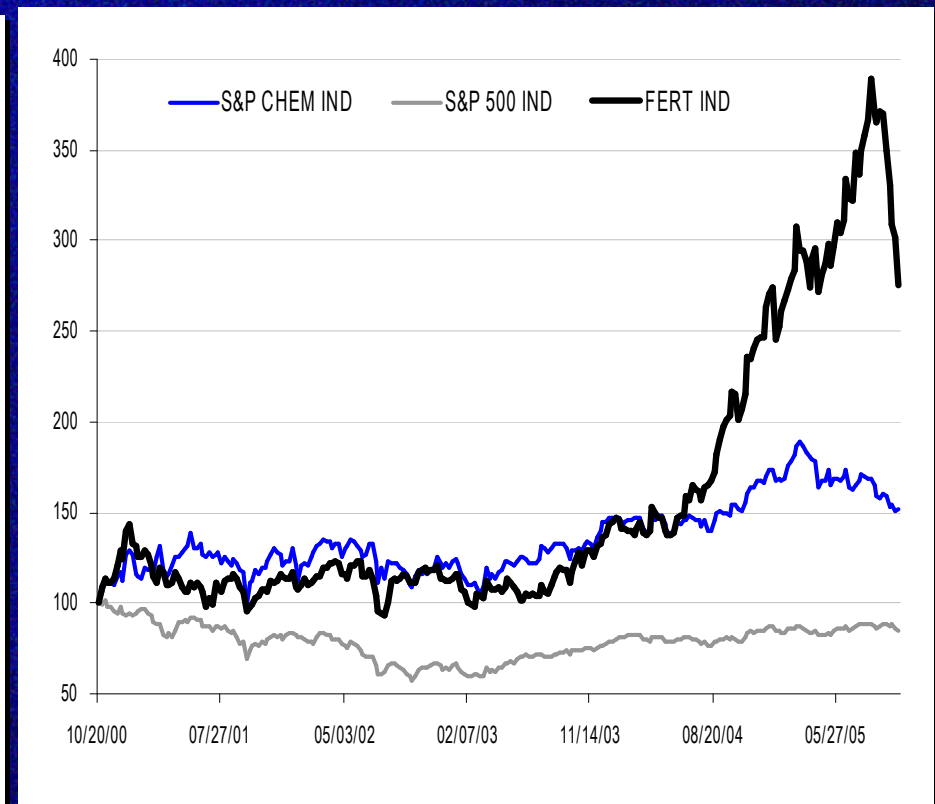
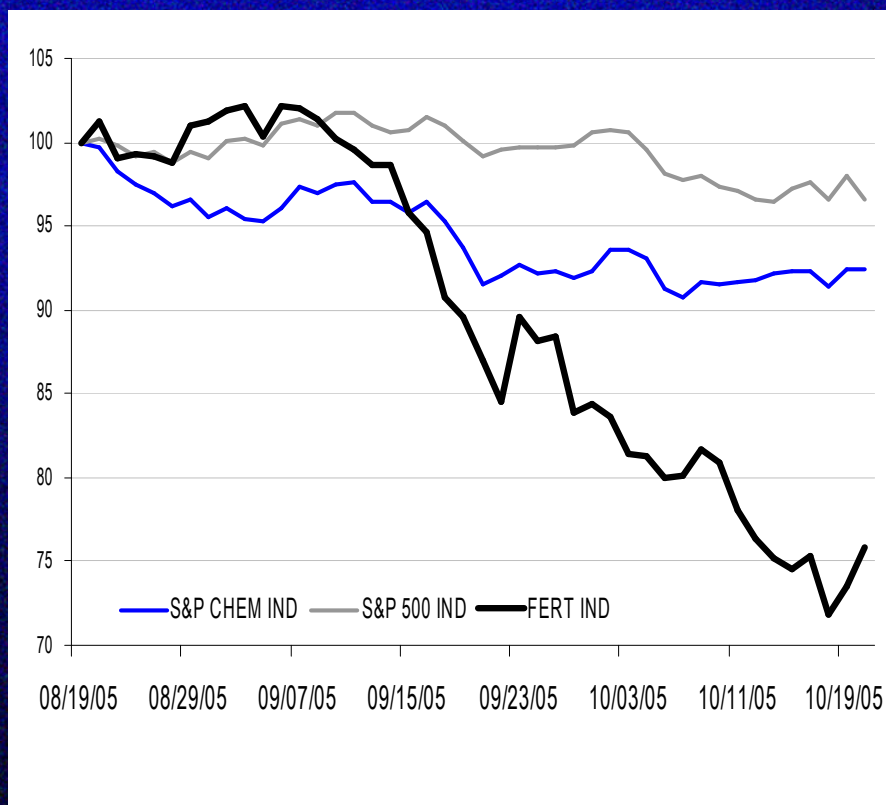
Source: Bloomberg





# Fertilizer Sector Has Been Under Pressure in Recent Months

## ...But Out-Performed Broader Market In Recent Years



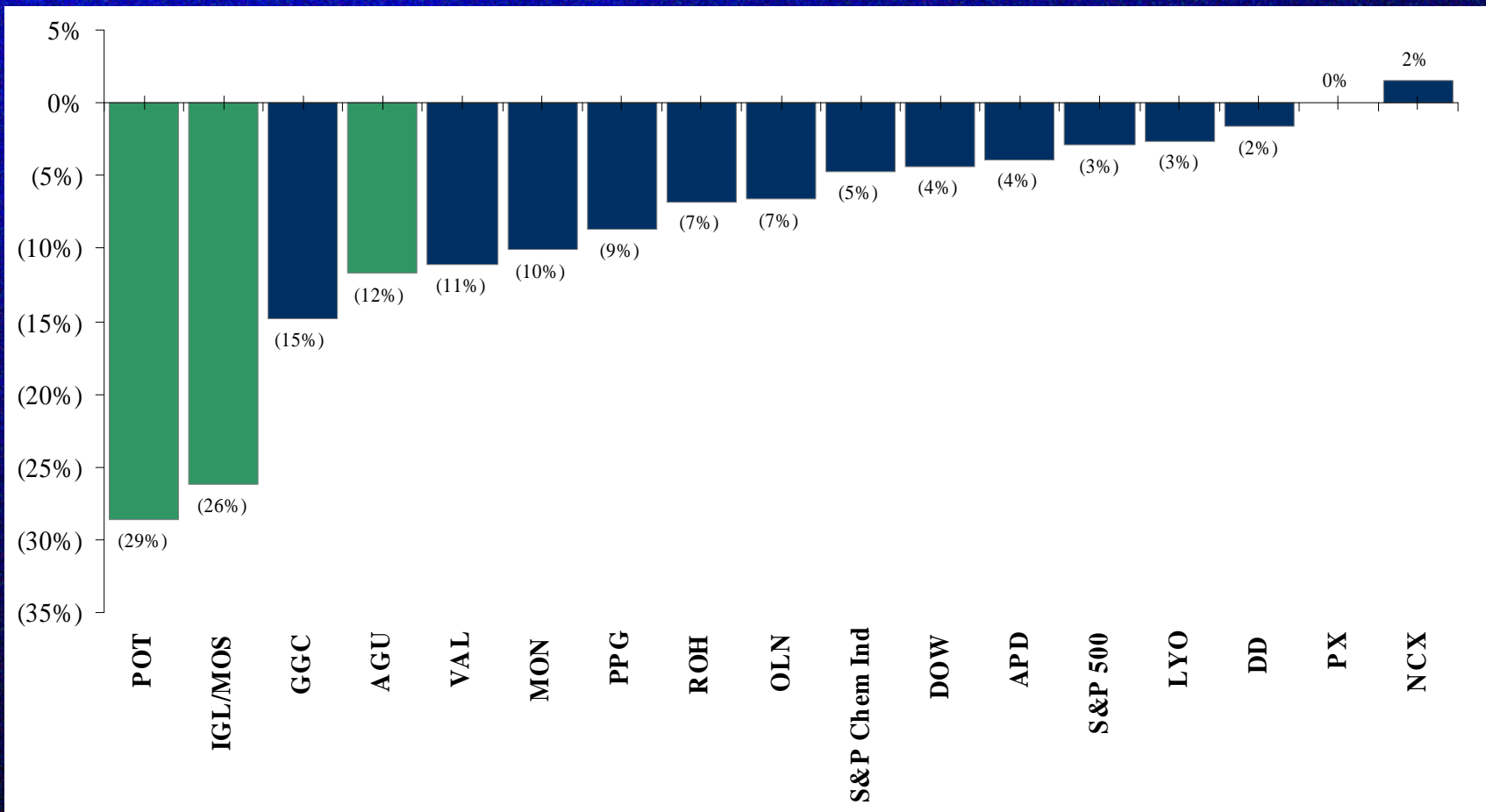
Source: Factset, ML Estimates

Note: Fertilizer Index is market-cap weighted average of AGU, POT and adjusted IGL/MOS shares.





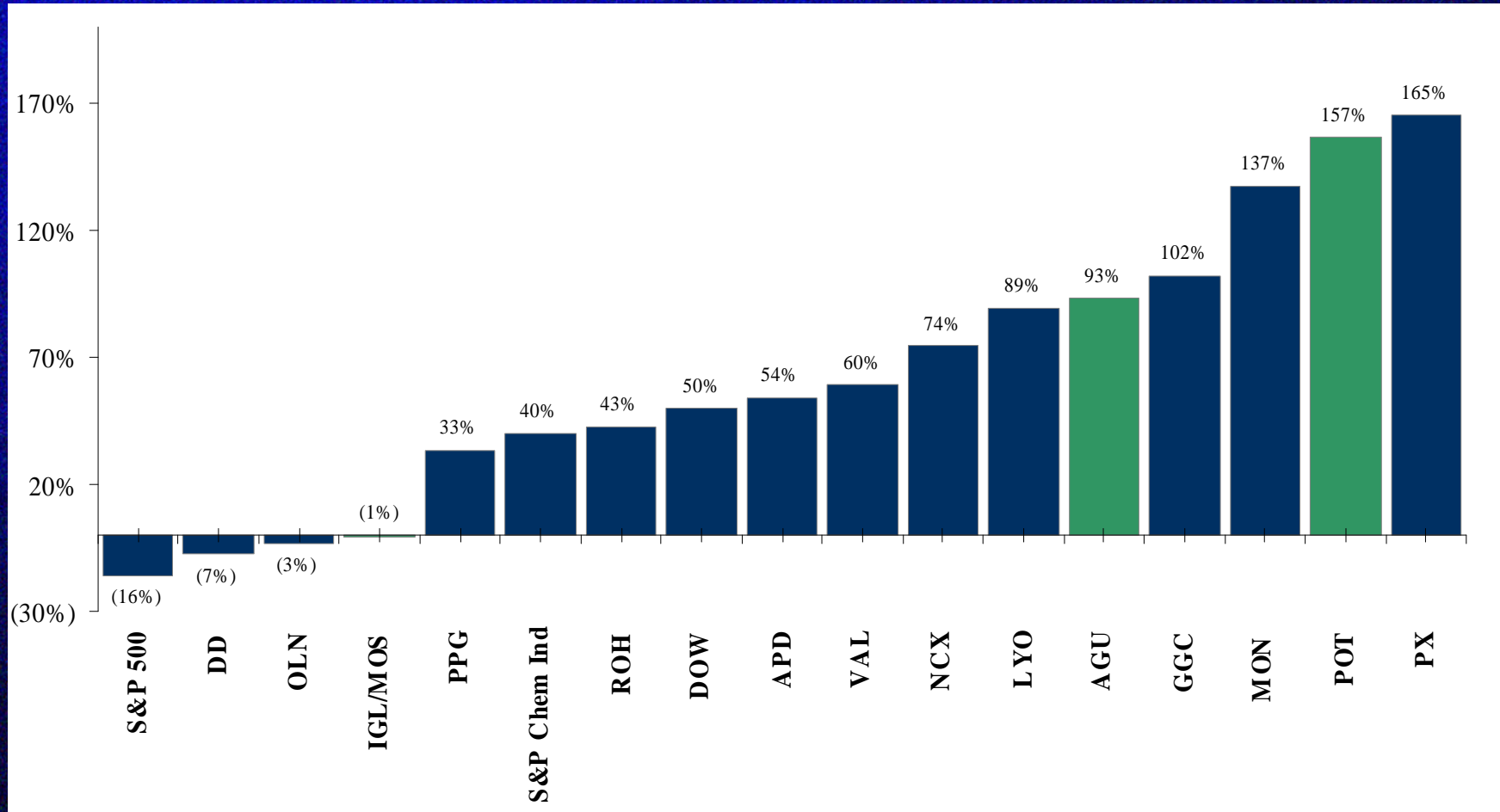
# 3-Month Share Price Performance



Source: Factset



# 5-Year Share Price Performance



Source: Factset



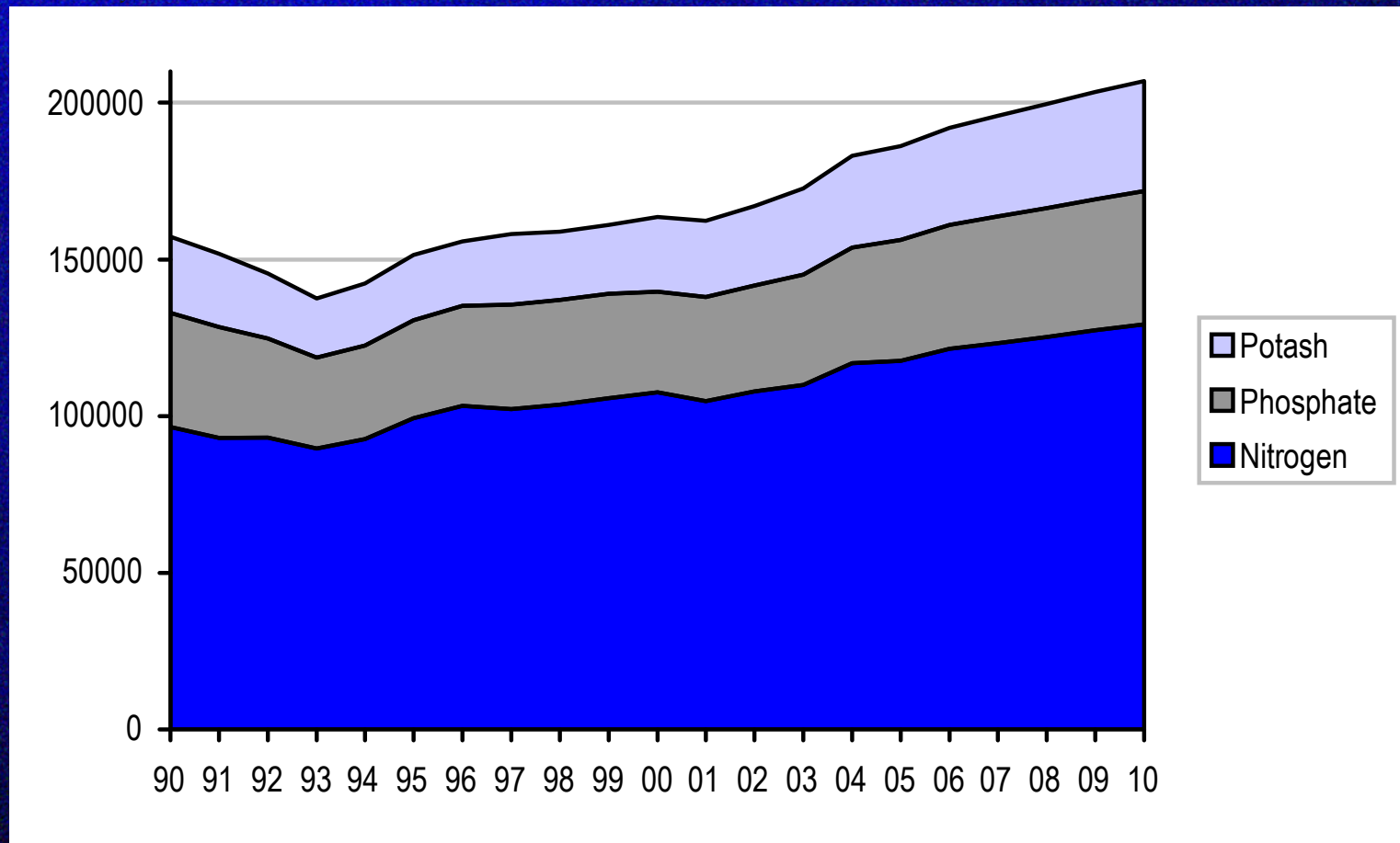
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# Global Fertilizer Demand Trends Remain Positive

(k mt of K<sub>2</sub>O, P<sub>2</sub>O<sub>5</sub>, and N)

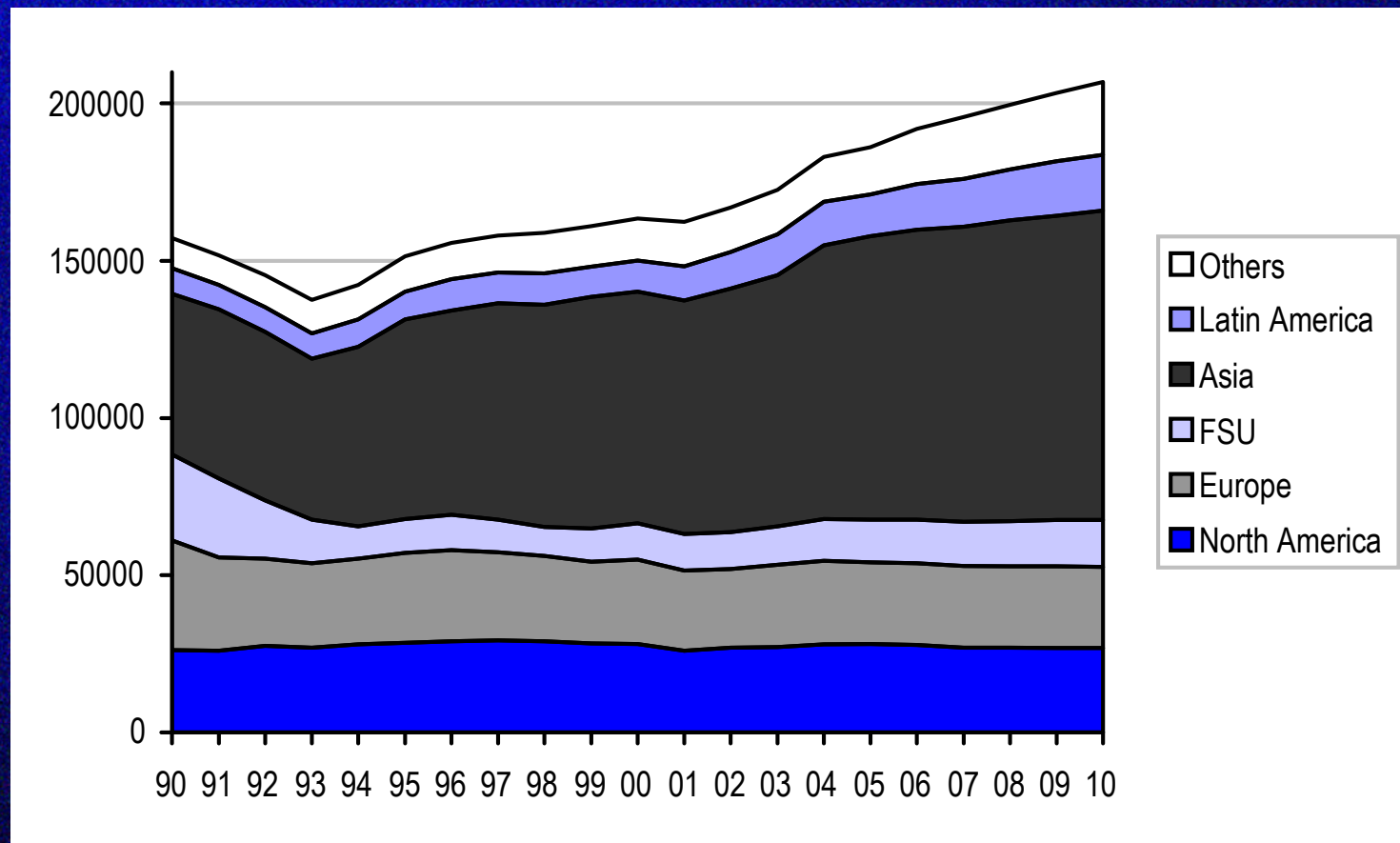


Source: Fertecon



## .... Driven By Asia

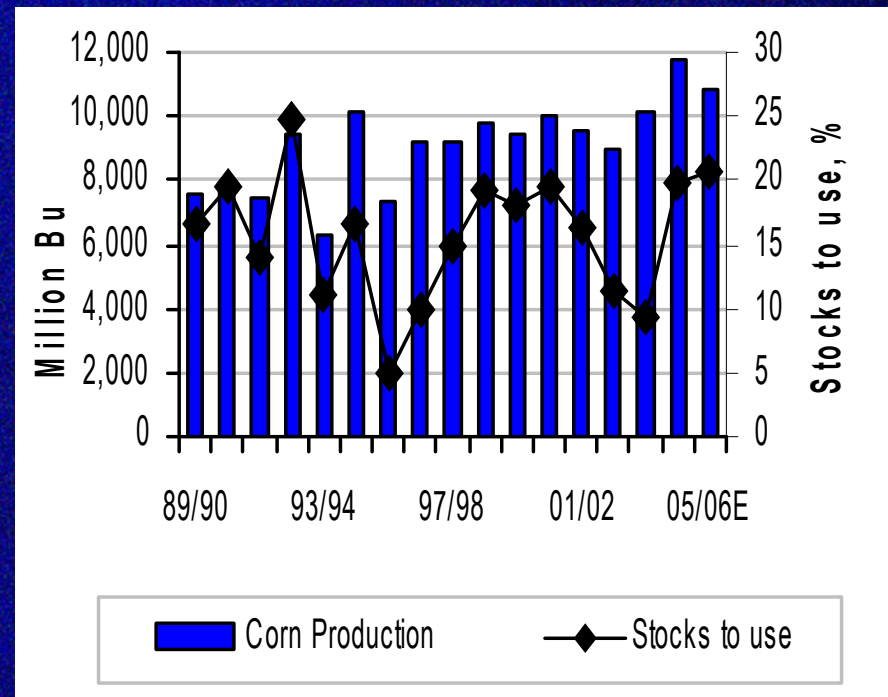
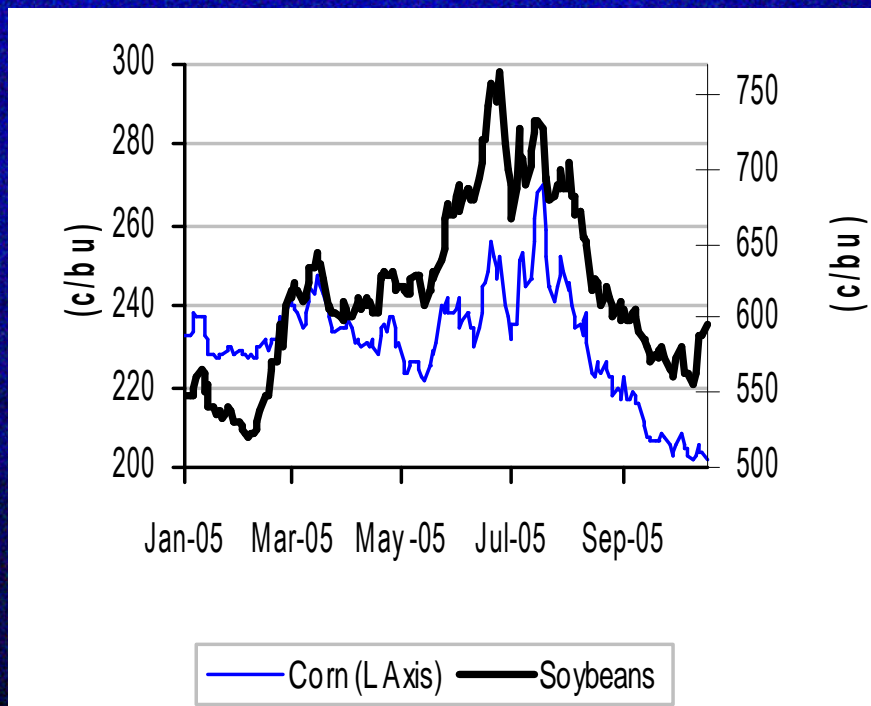
*(k mt of K<sub>2</sub>O, P<sub>2</sub>O<sub>5</sub>, and N)*



Source: Fertecon



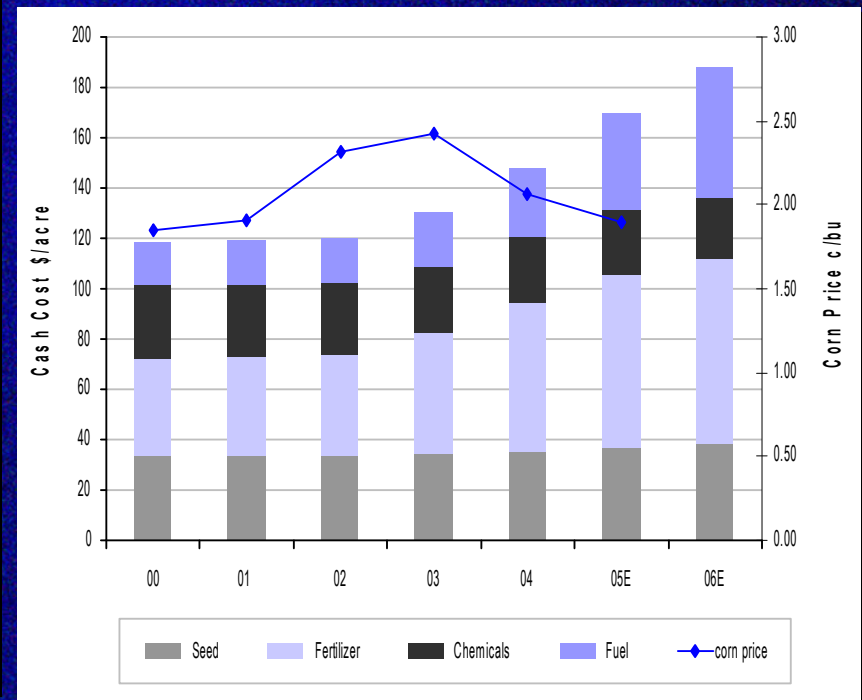
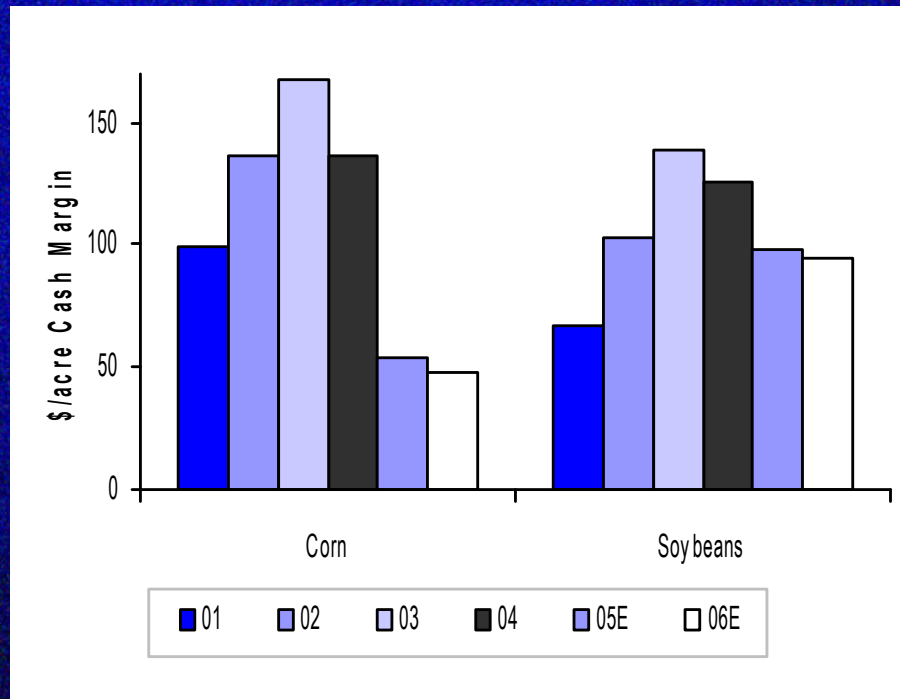
# Near-Term Grain Outlook Is Challenging



Source: USDA, Bloomberg



# As Is Grower Margin Outlook With Rising Input Costs

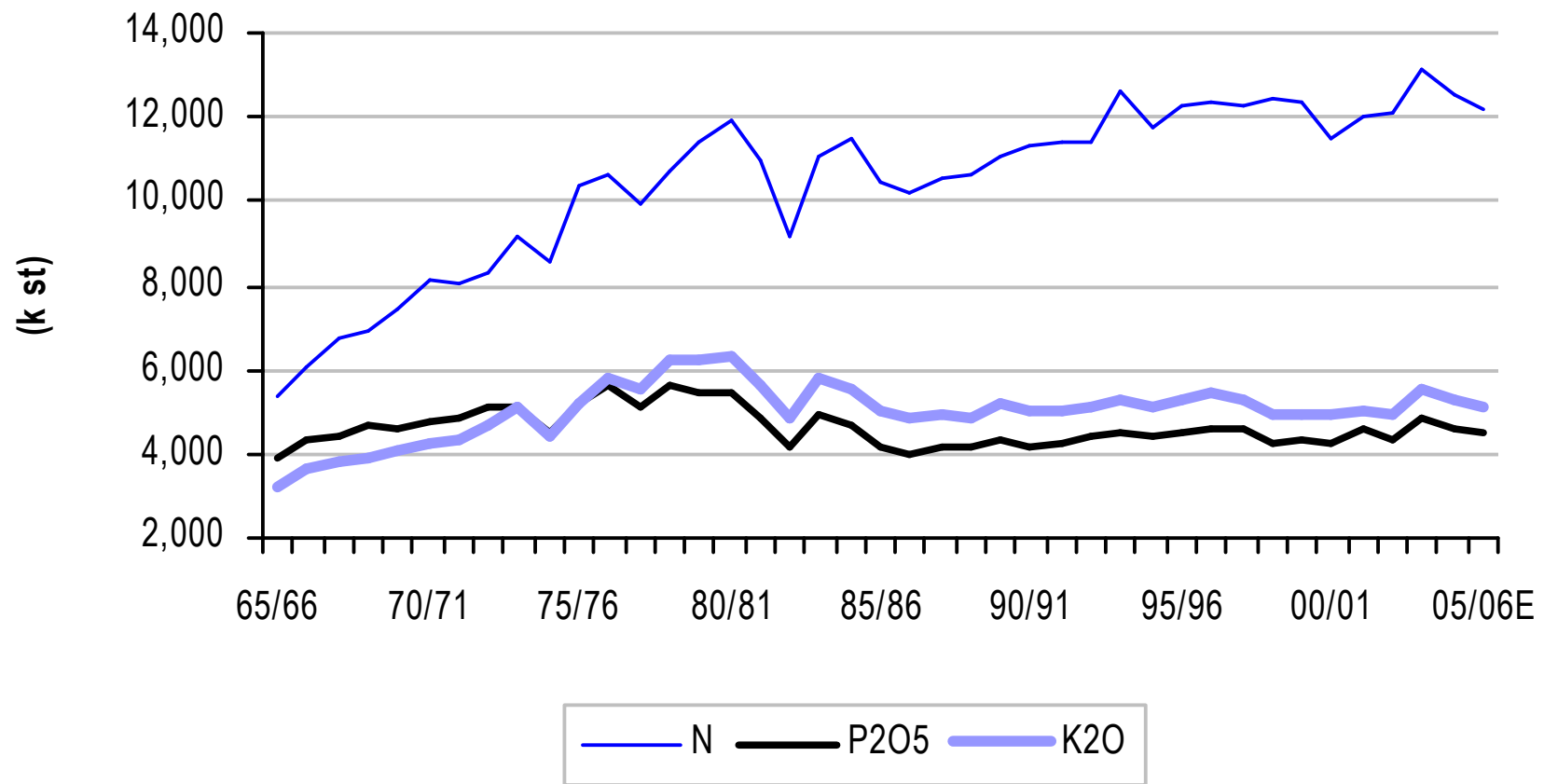


Source: USDA and ML Estimates



# U.S. Fertilizer Demand Could Fall 3-5% In 05/06

But Has Been Relatively Stable In The Last 10 Years

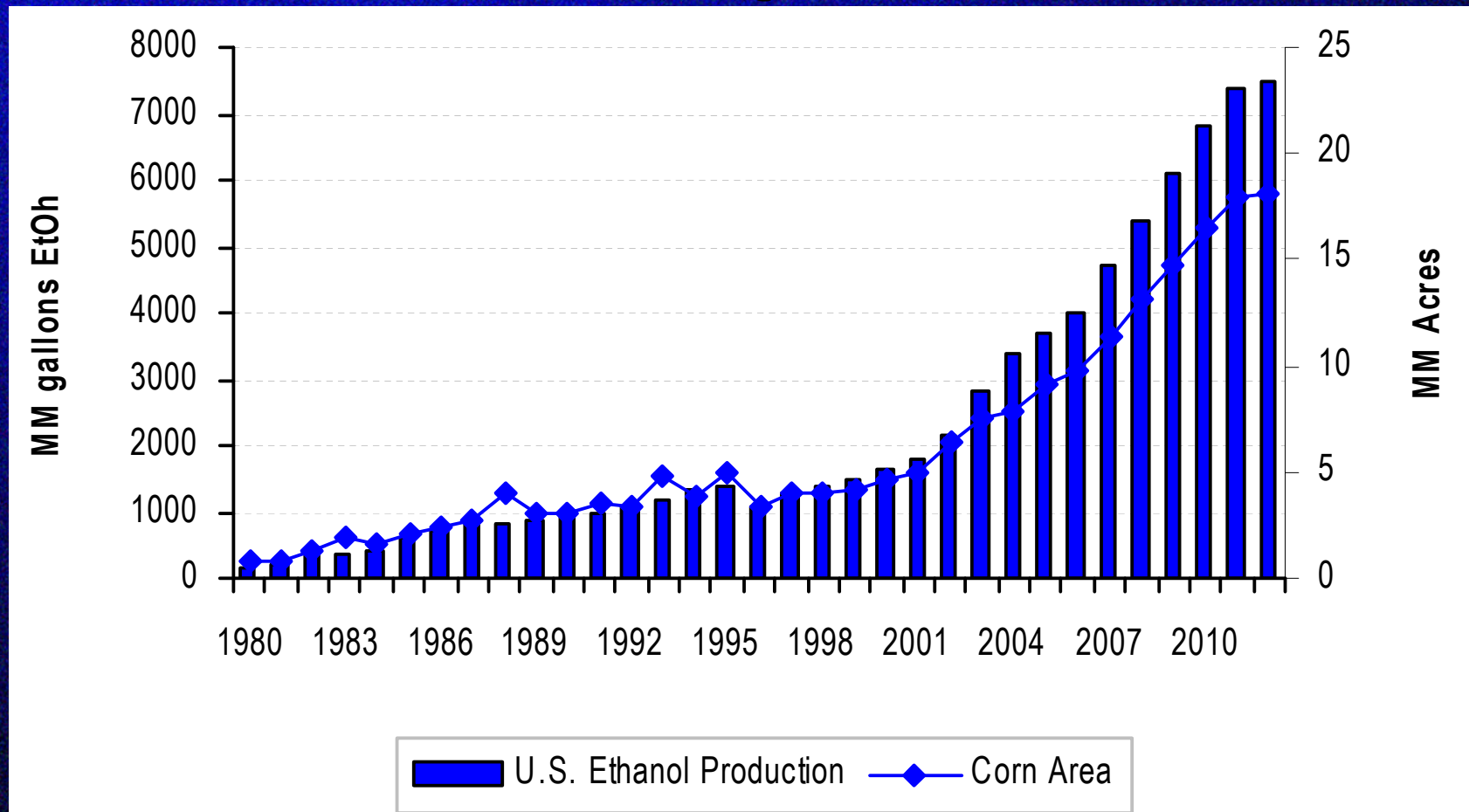


Source: AAPCO and ML Estimates



# But Longer Term Corn Outlook Positive

## Ethanol Boosting U.S. Corn Demand

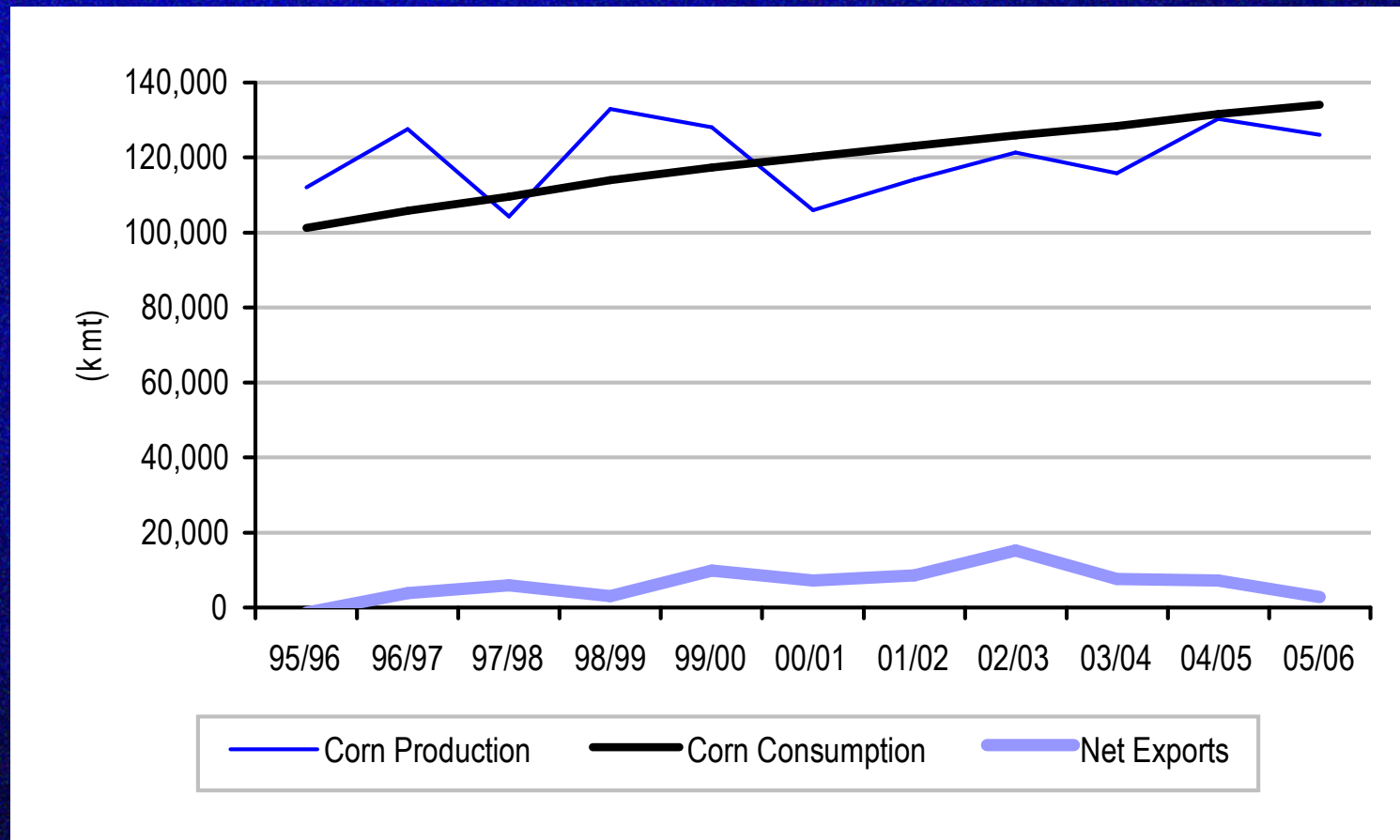


Source: RFA and ML Estimates



# China Could Become A Net Corn Importer In 06/07

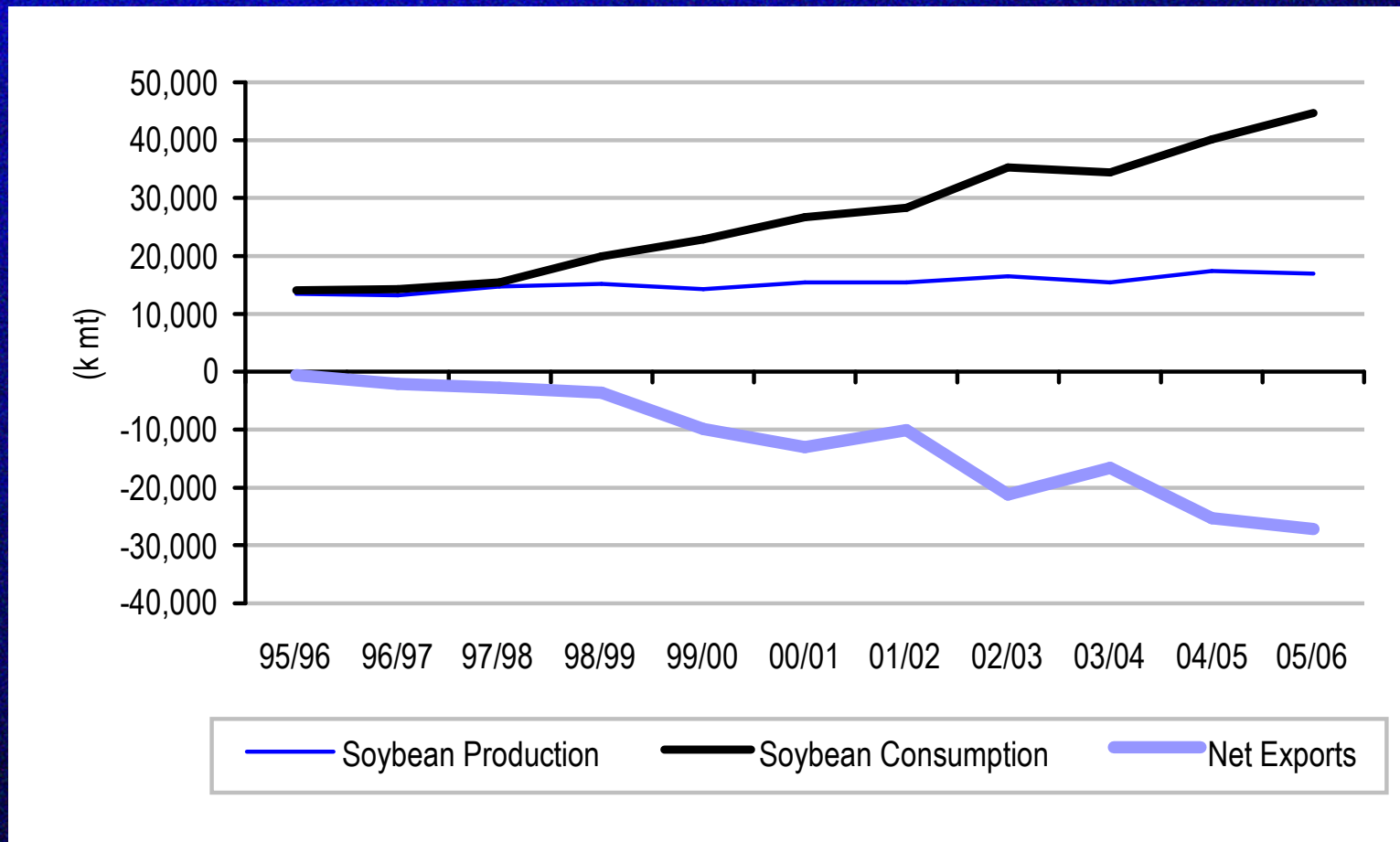
## Beneficial To U.S., the Leading Corn Producer



Source: USDA



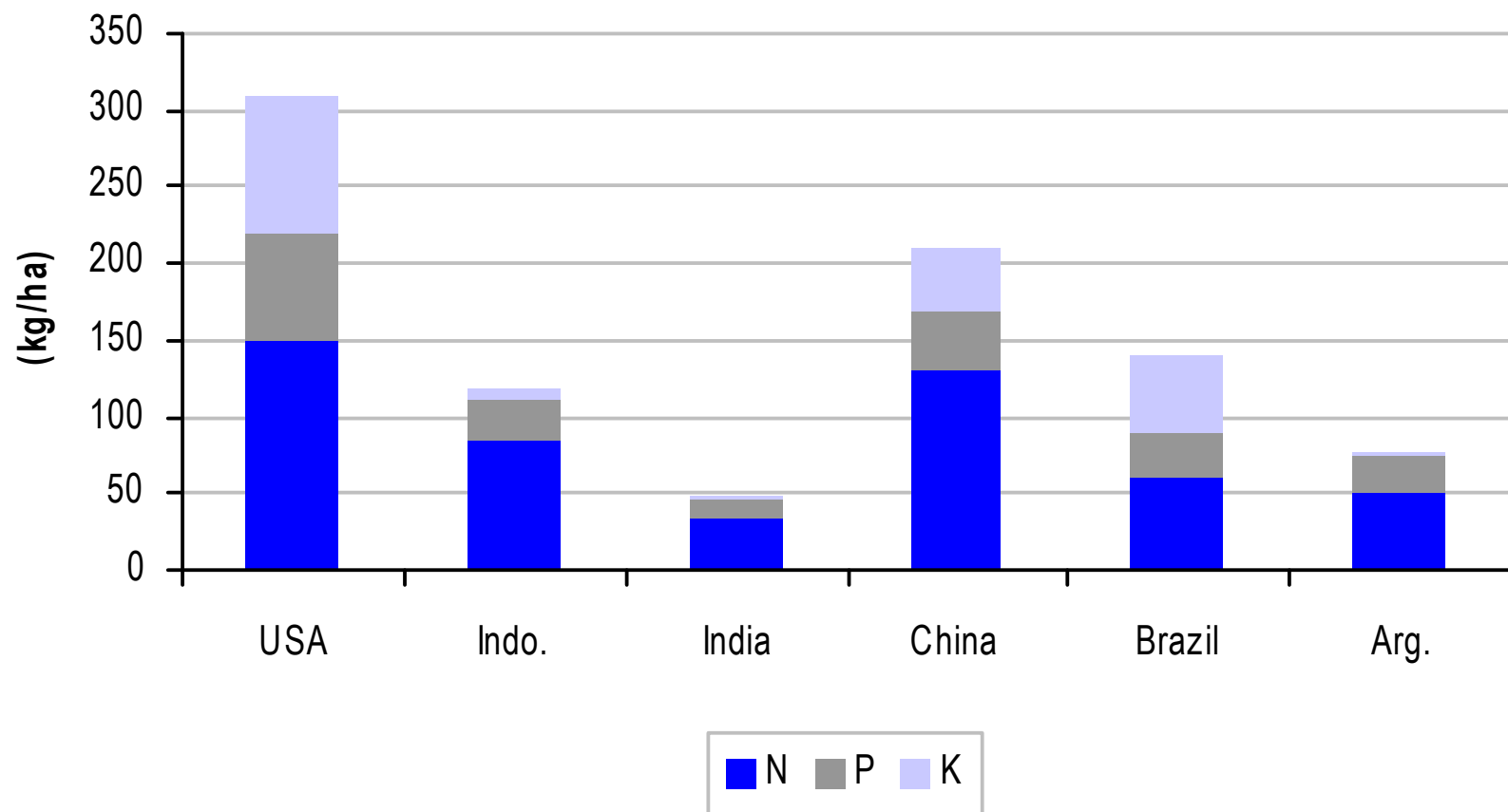
## Unlike Soybeans Where Brazil Has Benefited



Source: USDA



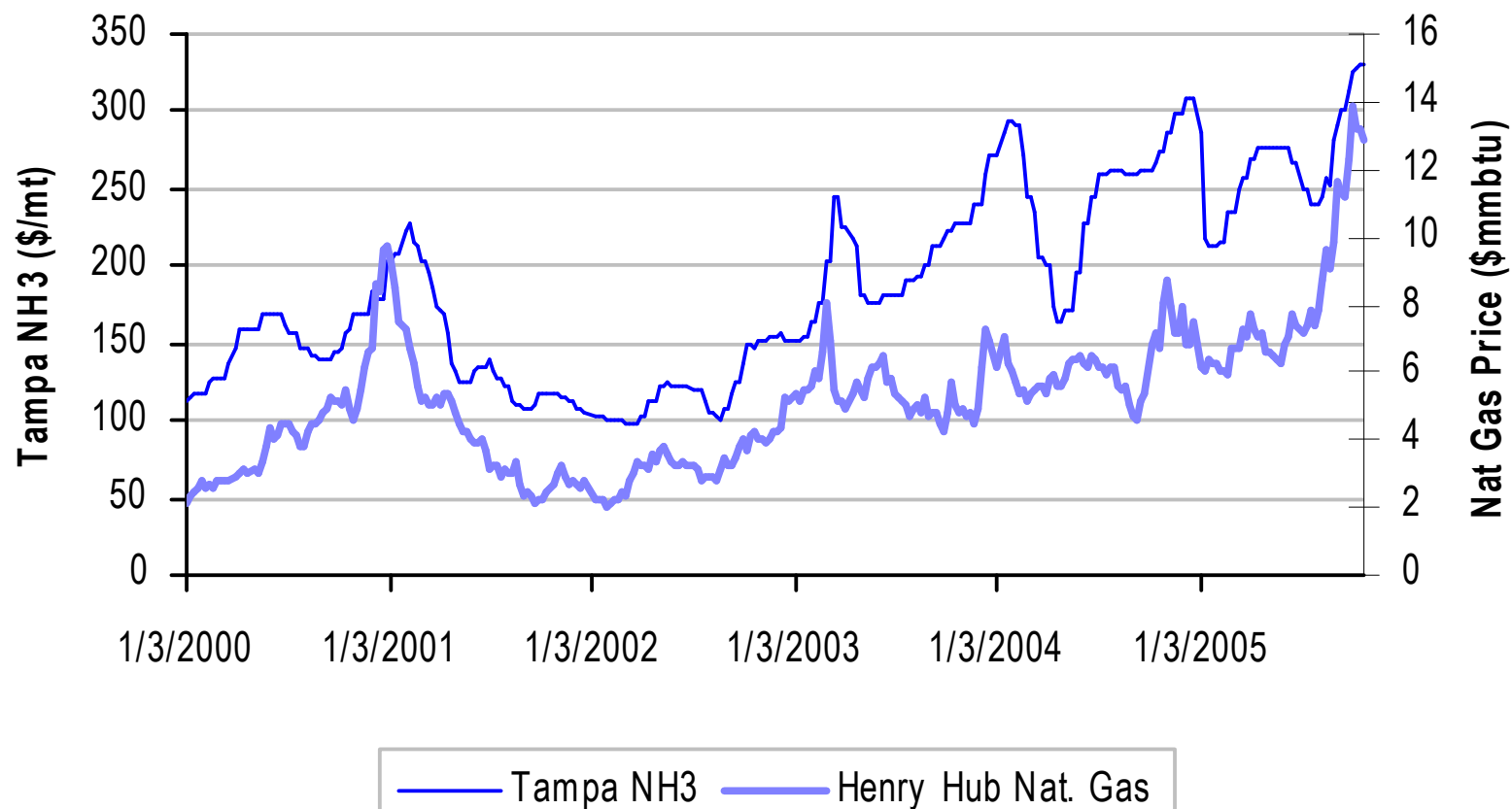
# Potential Exists For Significantly Higher Fertilizer Demand in Asia and South America



Source: IFA, USDA and ML Estimates



# Tampa Ammonia Prices In Record Territory, In Line With Natural Gas

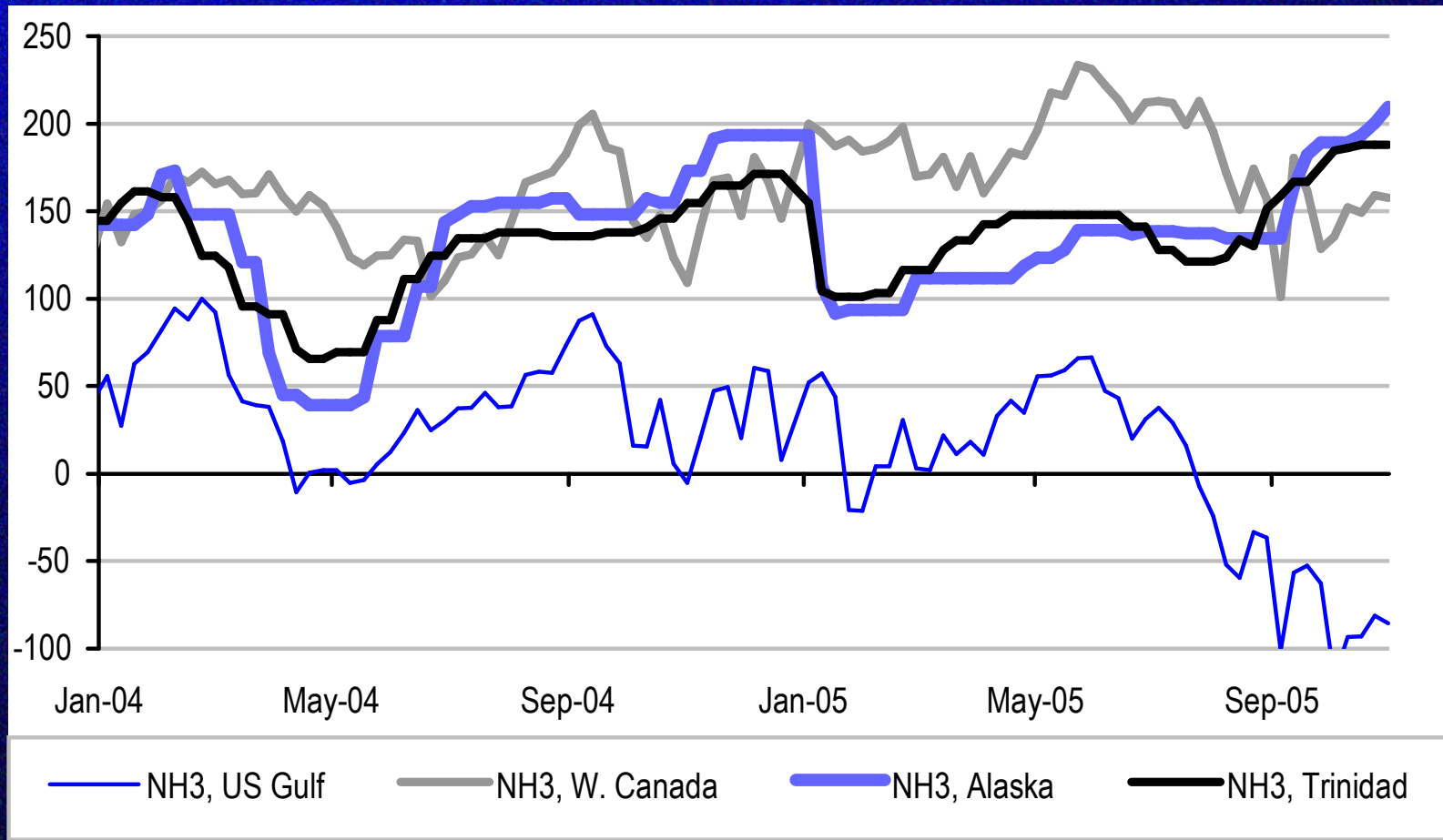


Source: Green Markets and Bloomberg



# Near-Term NH<sub>3</sub> Capacity Shutdowns Could Lead To Higher Prices

(cash margin, \$/st of product)

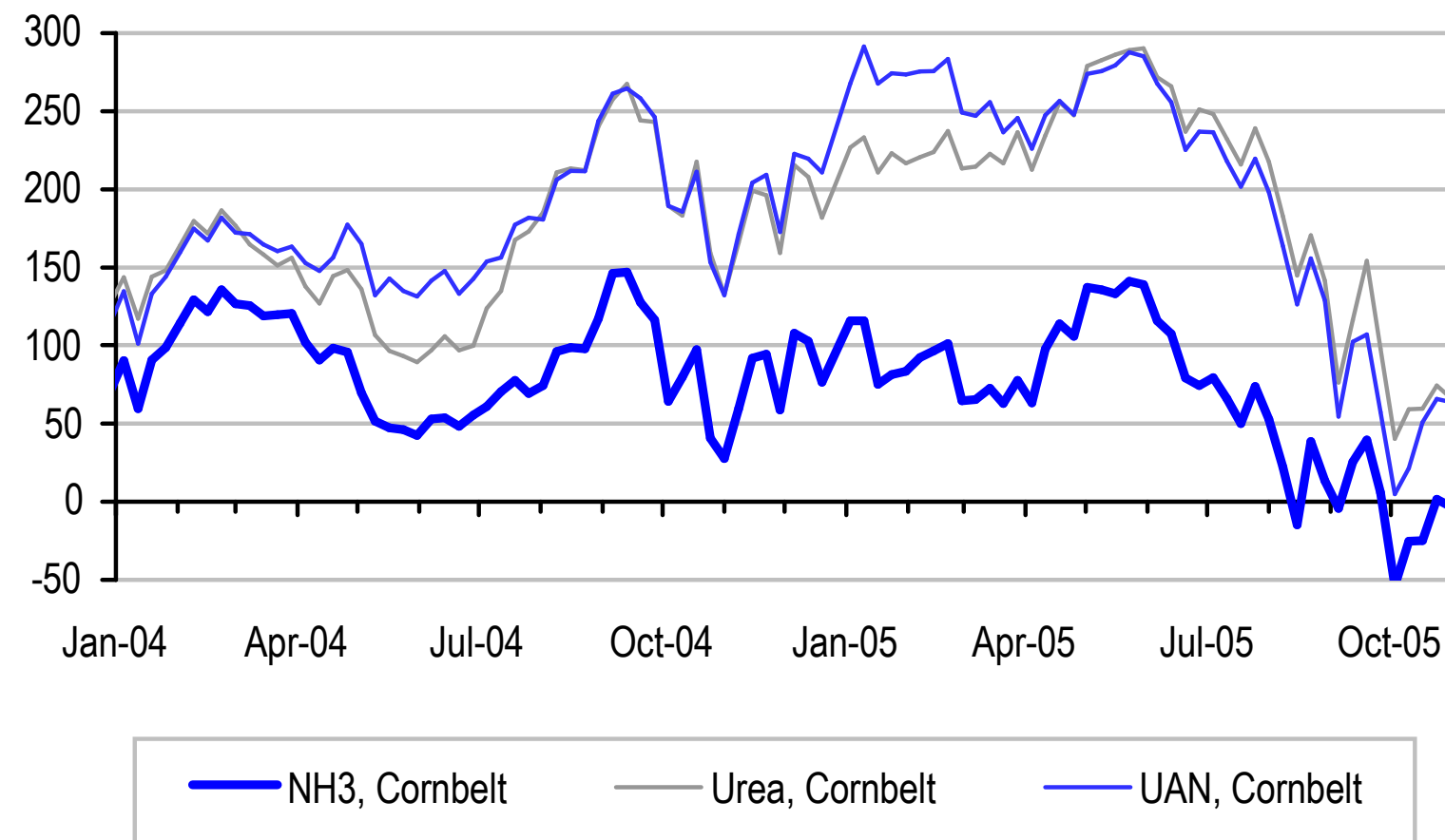


Source: Green Markets, Bloomberg and ML Estimates



# Mid-Cornbelt Margins Under Pressure For All Nitrogen Products

(cash margin, \$/st as nitrogen)

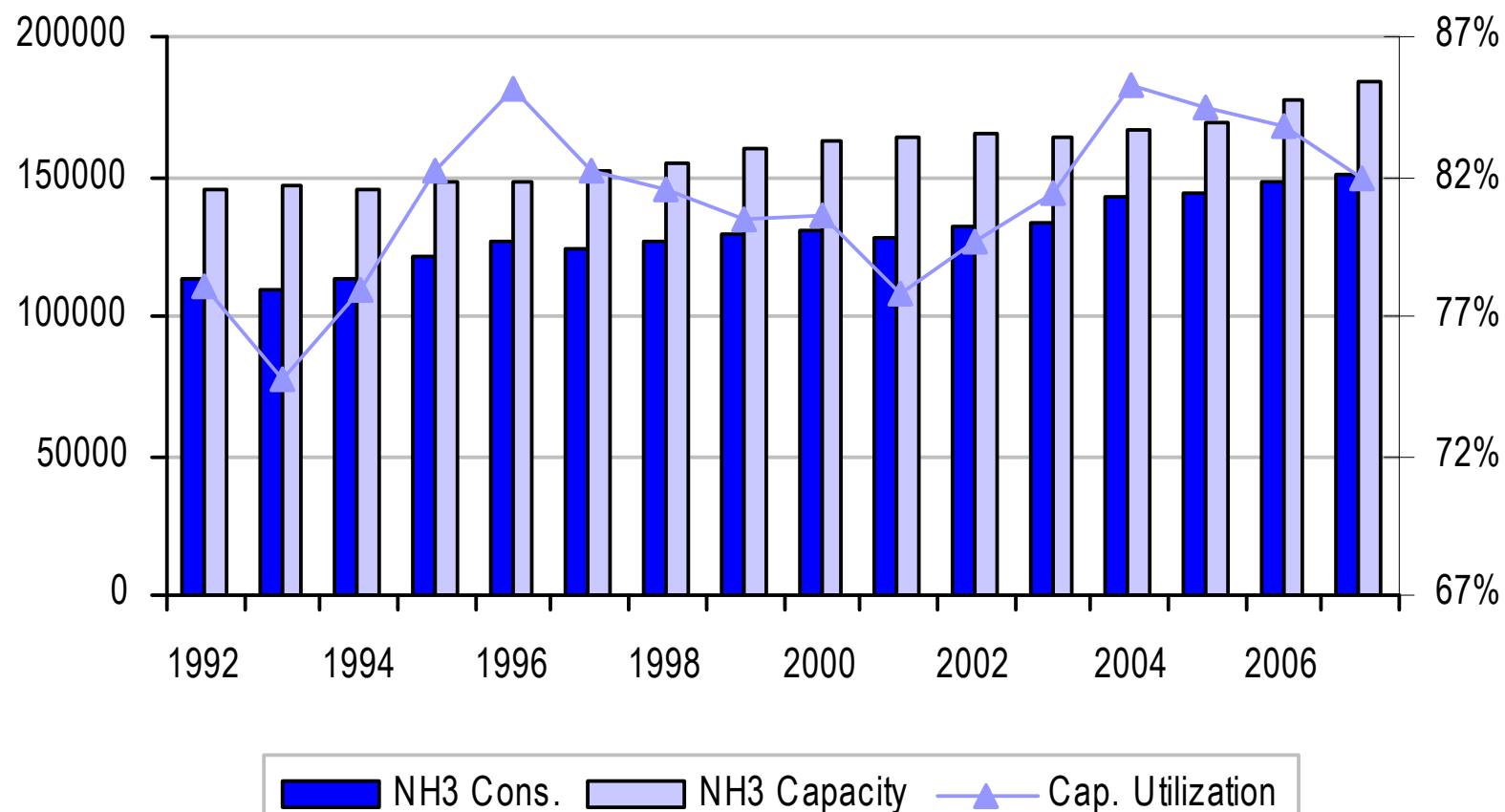


Source: Green Markets, Bloomberg and ML Estimates



# Ammonia Cap. Utilization Could Decline In 2006 But Remain Near Peak Levels From Mid-1990s

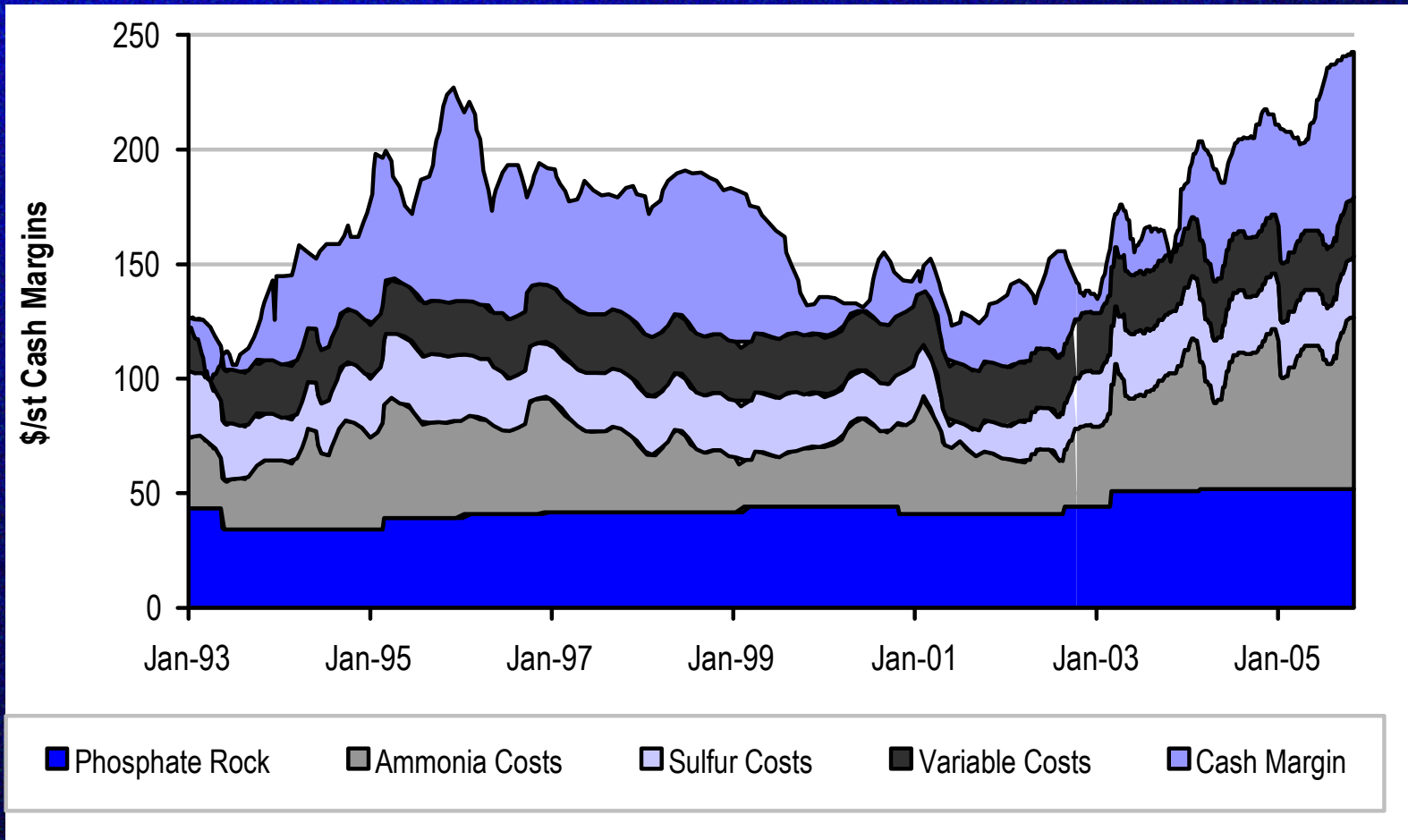
(k mt of product)



Source: Fertecon



# DAP Cash Margins Approaching Peak 1995 Levels

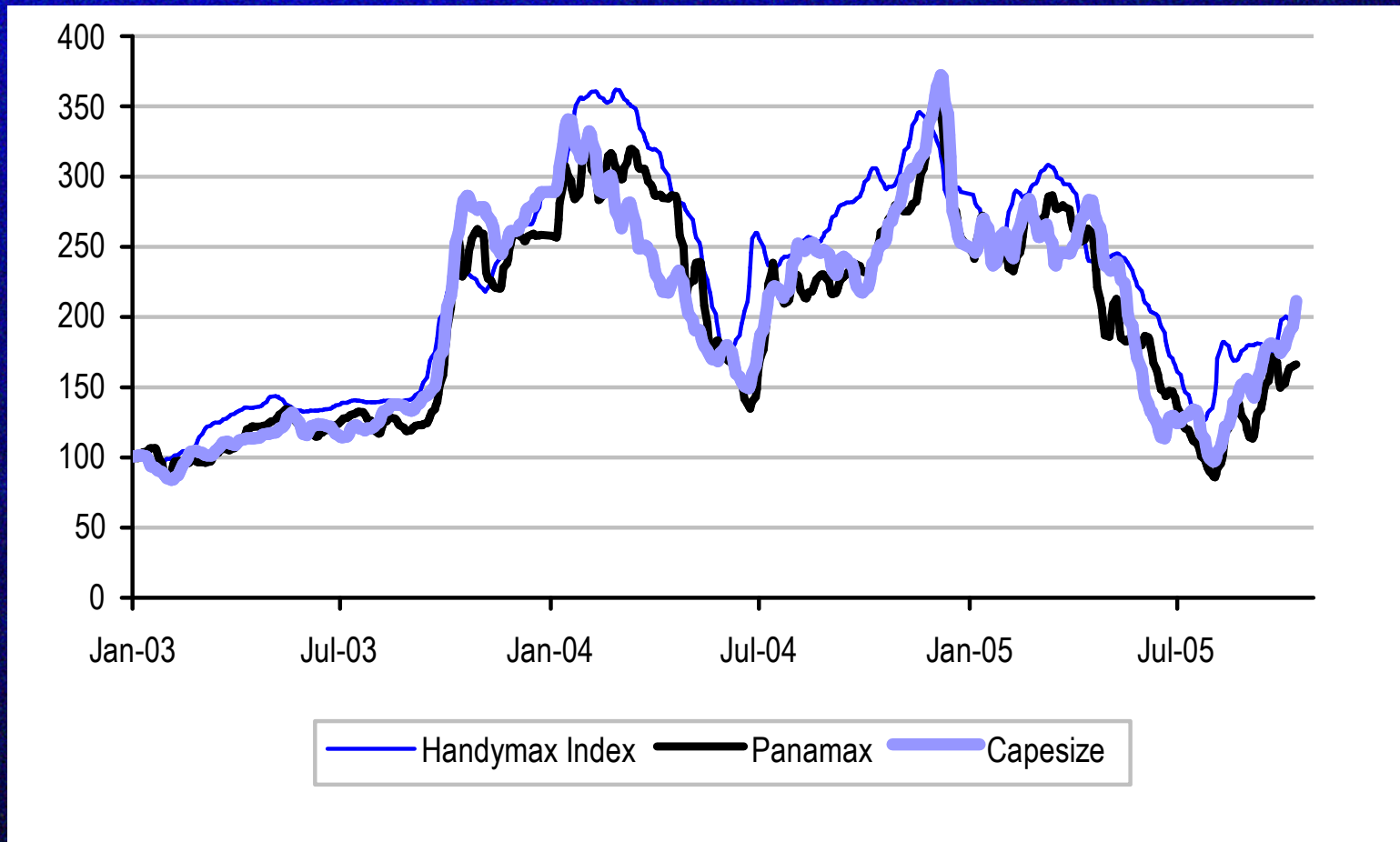


Source: Green Markets and ML Estimates



## ... But DAP Margins Under Near-Term Pressure From Rising Ammonia, Sulphur, and Freight Costs

(normalized Baltic Dry Index)

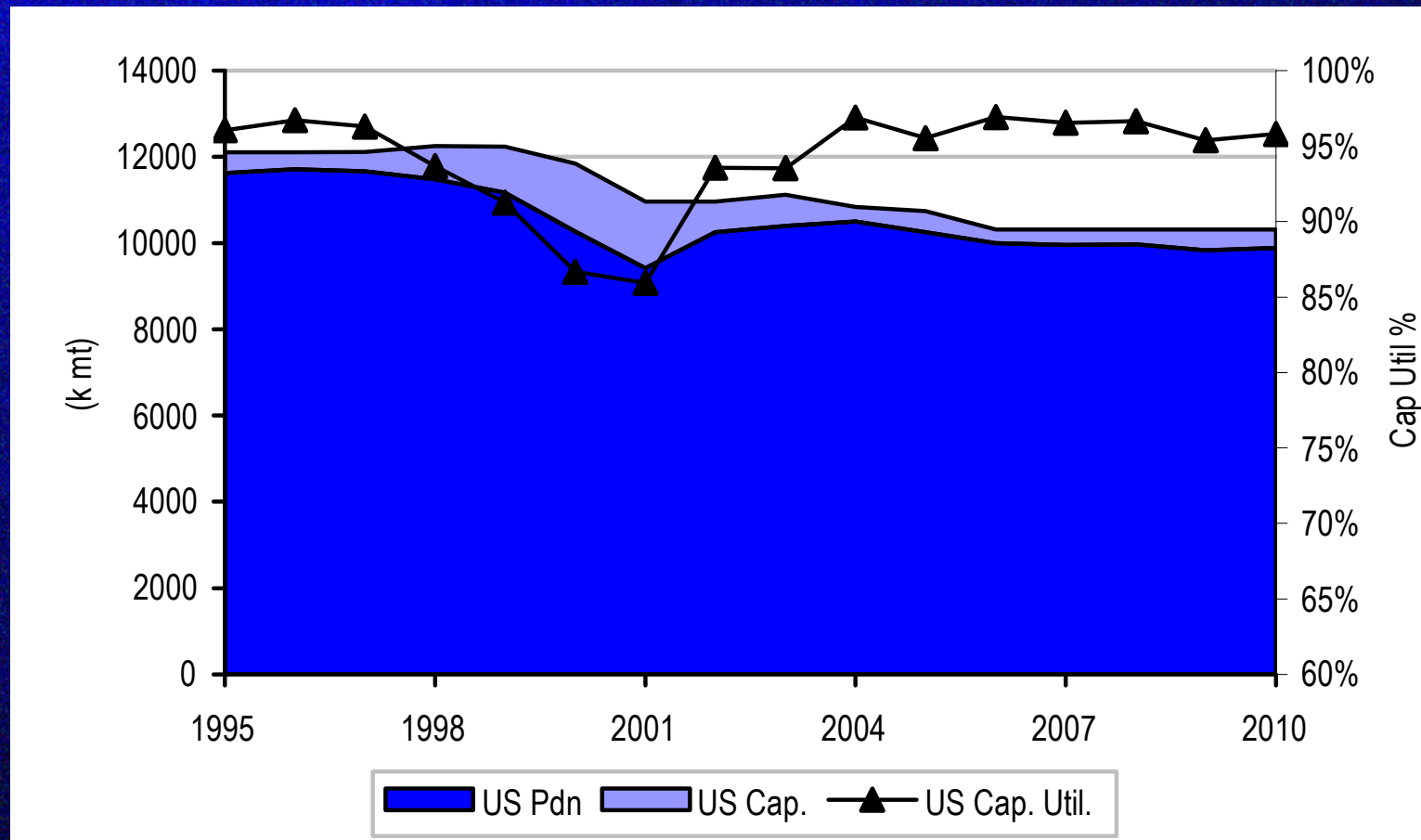


Source: Bloomberg



# Favorable 2006 Outlook For US Phosphate Industry

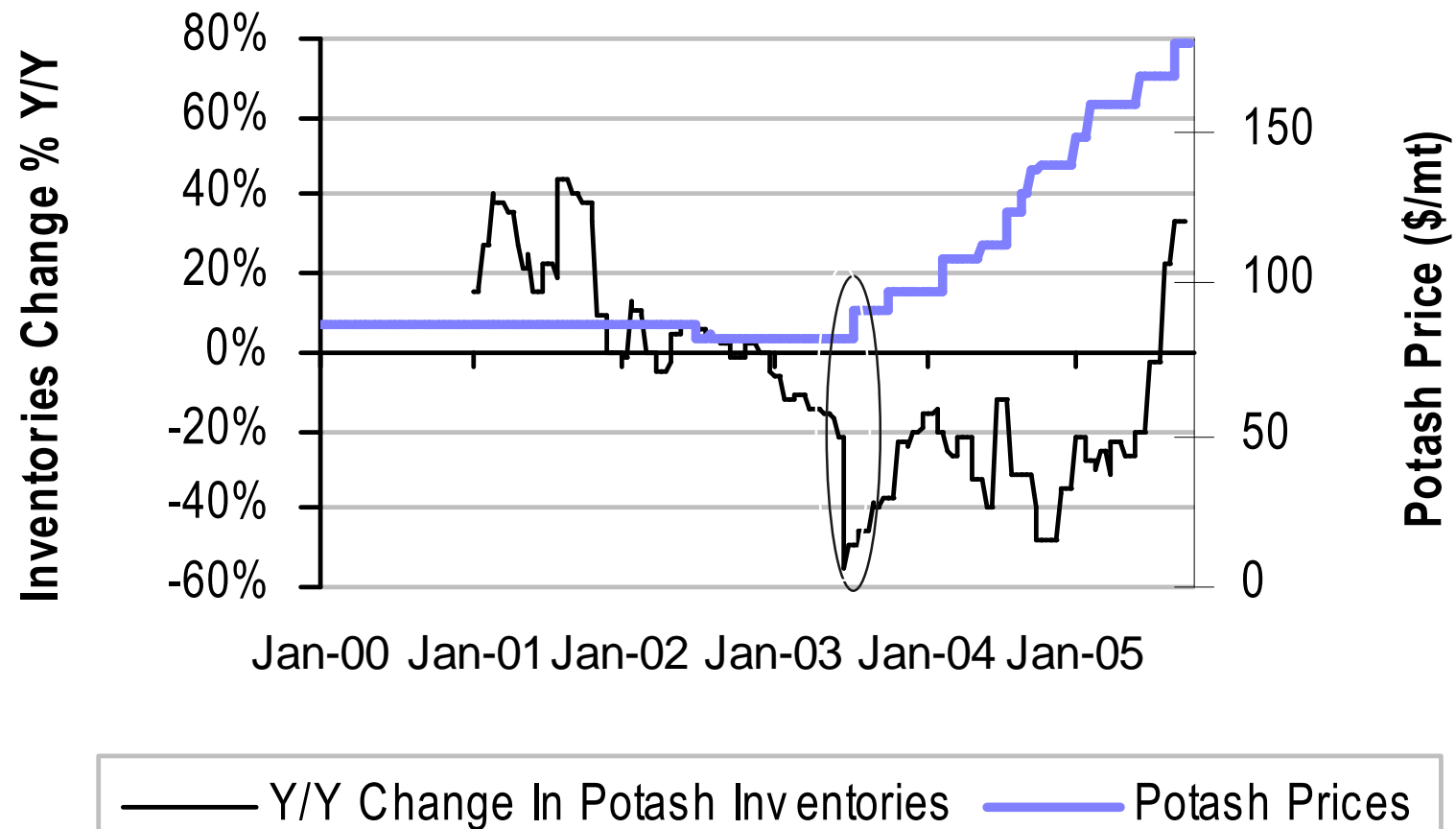
Cap. Utilization Has Returned To Tight Conditions of Mid-1990s



Source: Fertecon Research Centre and ML estimates



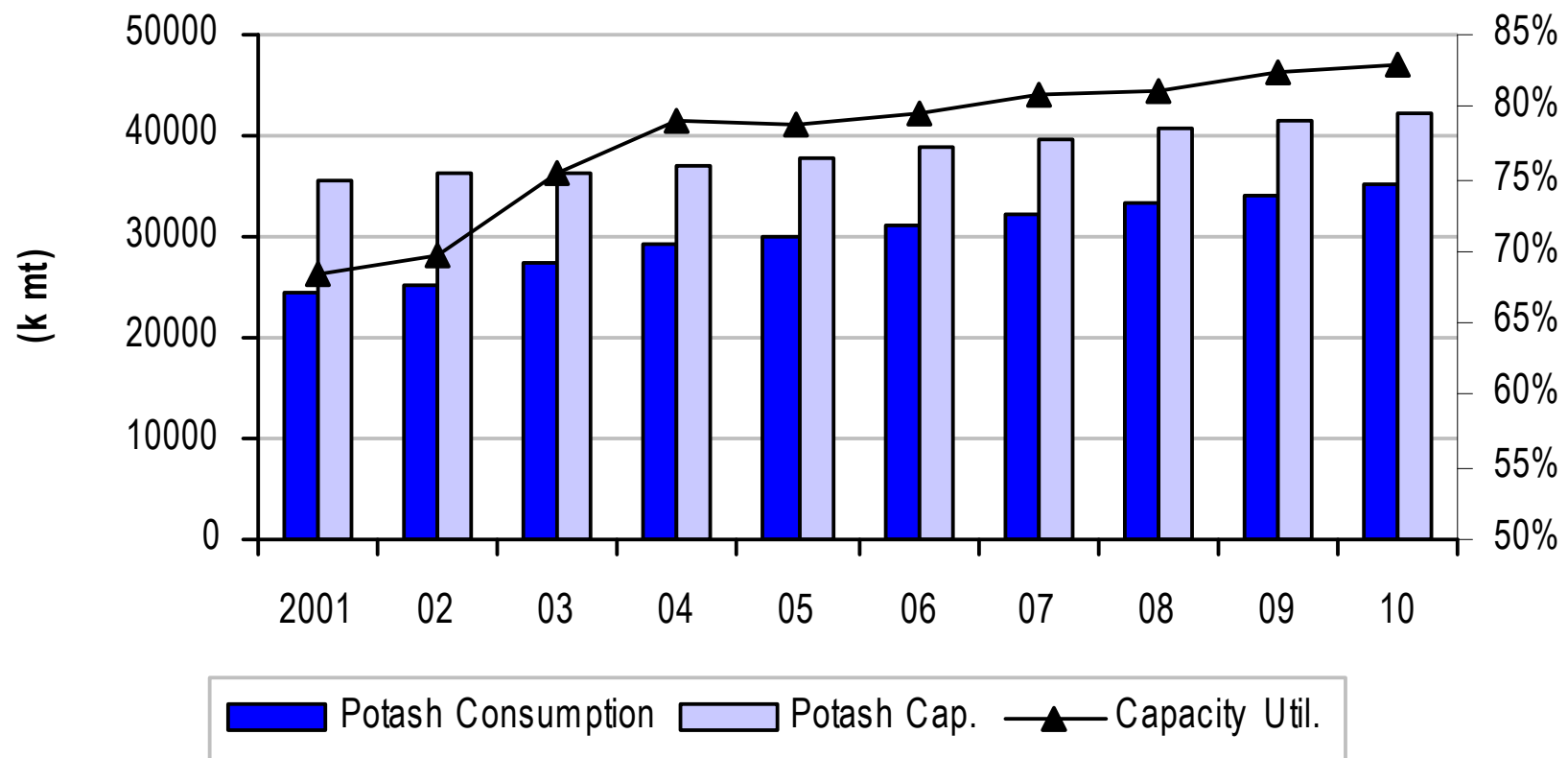
# Do North American Potash Inventories Signal Inflection Point In Potash Price Movement?



Source: TFI, Green Markets



# Potash Supplies Could Remain Tight For Several Years



Source: Fertecon

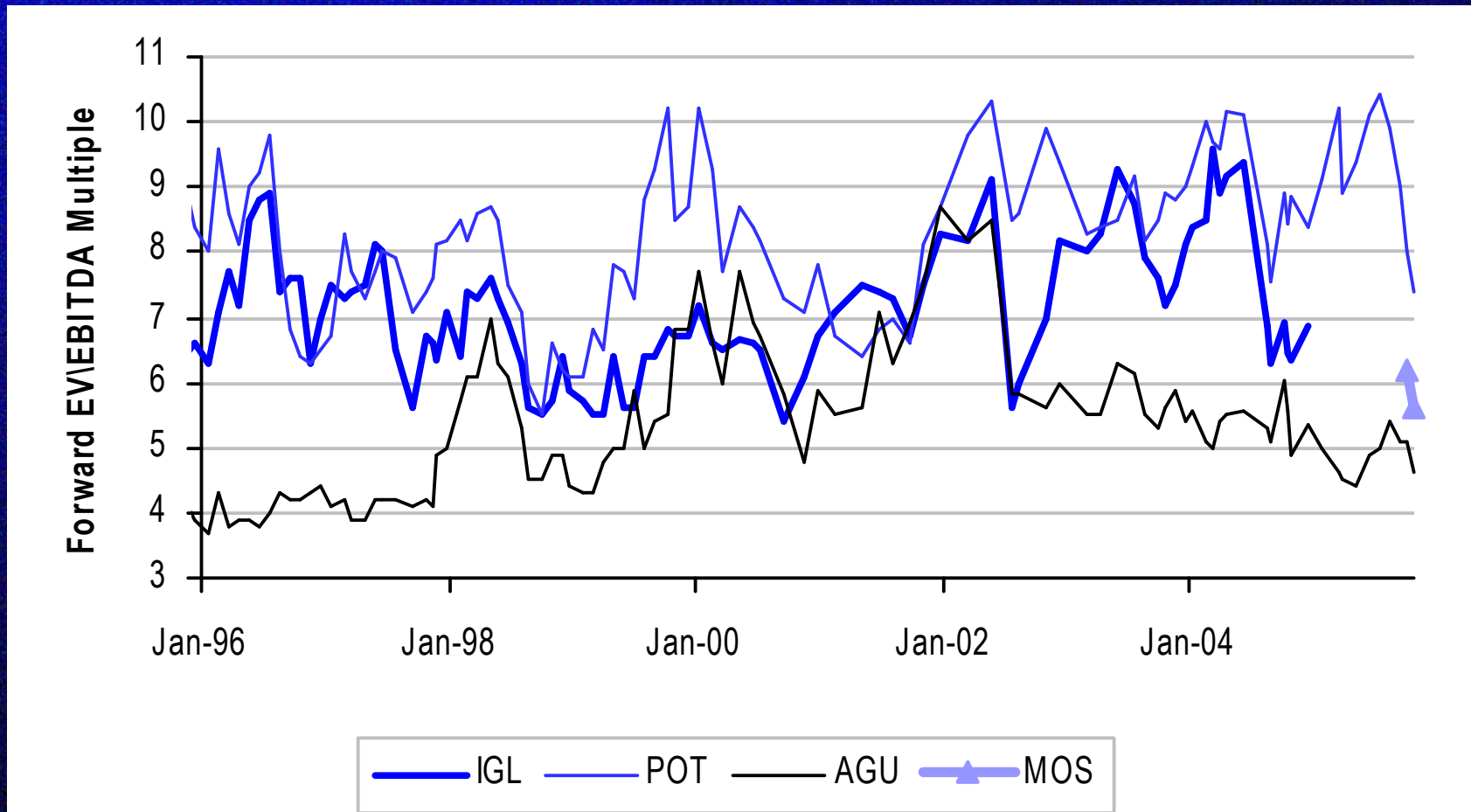


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# Wide Disparity Between Fertilizer Stock Valuations



Source: ML Estimates



# Earnings Leverage Varies By Producer

	2006E Volume (000 st)	EPS Impact of \$10/st Margin Change	% of 2006E EPS
<u><b>Ammonia</b></u>			
Potash Corporation	2,070	\$0.11	2%
Agrium	1,690	\$0.09	4%
<u><b>Urea &amp; UAN</b></u>			
Agrium	4,140	\$0.21	10%
Potash Corporation	3,825	\$0.23	3%
<u><b>Phosphate</b></u>			
Mosaic	12,550	\$0.17	10%
Potash Corporation	4,230	\$0.25	4%
Agrium	1,260	\$0.06	3%
<u><b>Potash</b></u>			
Potash Corporation	10,470	\$0.42	7%
Mosaic	9,350	\$0.08	5%
Agrium	2,090	\$0.07	3%

Source : ML Estimates





# Fertilizer Nutrient EV/EBITDA Multiples

	<u>Valuation Multiples By Nutrient (EV/EBITDA)</u>	<u>Greenfield Plant Lead Time</u>	<u>Raw Material Cost Volatility</u>	<u>Industry Consolidation</u>
<u>Potash</u>	~8-9x	5 yrs	Low	High
<u>Phosphate</u>	~7-8x	4 yrs	Med	Med, Increasing
<u>Nitrogen</u>	~4-5x	3 yrs	High	Low, Increasing

Source: ML Estimates





# Fertilizer Sector Investment Positives

- Global Demand for Fertilizer Increasing Steadily
  - ▶ Increased demand for grain driven by animal feed and EtOH
- Ag cycles are somewhat independent from general economy
- Fertilizer price trends are reasonably predictable
- Fertilizer producers have high operating leverage to margin gains
- Favorable consolidation trends in P and K



# Fertilizer Sector Investment Concerns

- Compressed farm cash margins could lead to reduced or delayed fertilizer applications
- Challenges in Brazilian ag economy could be slow to reverse
- Bird flu concerns could lower feed grain demand
- Nutrient Specific
  - ▶ Potash – FSU Capacity expansions and further slowdown in price momentum
  - ▶ Phosphate – Margin pressure from ammonia and sulphur
    - Ongoing capacity expansions in China
  - ▶ Nitrogen – Sustained high natural gas prices



# Merrill Lynch Investment Opinions

<u>Company</u>	<u>Ticker</u>	<u>Rating</u>	<u>Price</u>
Air Products	APD	B-1-7	\$57.44
Dow	DOW	C-1-7	\$45.60
DuPont	DD	A-1-7	\$41.81
Georgia Gulf	GGC	C-2-7	\$28.40
Huntsman	HUN	C-1-9	\$20.34
Lyondell	LYO	B-2-7	\$26.53
Monsanto	MON	C-1-7	\$63.35
Nova Chemical	NCX	C-2-7	\$36.19
Olin Corp.	OLN	B-2-7	\$17.99
PPG	PPG	C-2-7	\$59.80
Praxair	PX	B-1-7	\$49.13
Rohm and Haas	ROH	B-2-7	\$43.75
Valspar	VAL	B-2-7	\$21.76
United Agri Products	UAPH	C-2-7	\$19.06
Mosaic	MOS	C-1-9	\$13.63
Agrium	AGU	C-2-7	\$21.38
Potash Corp	POT	B-2-7	\$82.82



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