Magna International Inc. Stock Looks Poised to Rally 25%

Description

Magna International Inc. (TSX:MG)(NYSE:MGA) stumped the markets last week with a trifecta of good news: an earnings beat, an optimistic outlook, and a dividend hike. The stock is up nearly 12% since, but the rally may have just begun.

In fact, the optimistic price targets that some analyst firms have placed on Magna–Credit Suisse, for example, has a target of US$50, representing 25% upside from current prices–look achievable if you dig deeper into Magna's latest earnings report. Here's why.

The loonie factor

At first blush, Magna's sales figures disappoint:

- Fourth-quarter sales: down 3% year over year
- Full-year sales: down 7%

However, currency headwind–an uncontrollable factor–was the *only* reason why Magna's sales dipped because a stronger U.S. dollar translates into lower international revenues when converted. Excluding that, Magna's Q4 and 2015 sales grew 6% and 3%, respectively.

Moreover, Magna's light vehicle production volumes climbed in its largest markets, North America and Europe, last year, thanks to new programs by partner-customers, including the **Ford** Transit, Chevrolet Colorado, and **General Motors's** SUVs. That's encouraging, especially since Magna's production was feared to take a hit as the beleaguered Volkswagen counts among its top six customers.

While Magna foresees flat production volumes this year, it projects total sales to be between US$34.6 billion and US$36.3 billion. That translates into a nice 8% bump at the lower end. With the loonie starting to strengthen, the final number could look even better.

Rapidly growing profits

Magna's net income for 2015 was flat despite a 7% drop in revenue. Aside from a stronger U.S. dollar, restructuring lowered Magna’s costs and drove its margins higher. For example, the company aggressively sold some non-core businesses, such as battery pack and part of interiors, to slash unnecessary costs and boost profitability.

Meanwhile, the acquisition of automotive transmissions supplier Getrag in a deal worth nearly US$1.9 billion should give Magna huge headway in key growth markets like China.

These initiatives combined with rising sales should drive Magna’s profits even higher–its net income has doubled over the past five years.

Shareholders are being richly rewarded

For investors, rising profits mean higher returns from every aspect. The latest 14% increase in Magna’s quarterly dividend translates into a dividend yield of 2.5% at the current stock price, which is a nice top up to the company’s solid 23% return on equity. A robust share-repurchase program further adds to shareholders’ wealth while affirming management’s confidence in the company’s growth going forward.

Given the growth prospects, this could be a great entry point for investors as the stock appears to be at inflection point, poised to rally.

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Date
2025/07/28
Date Created
2016/03/02
Author
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