Is it Time to Buy These Auto Parts Suppliers?

Description

Magna International Inc.'s (TSX:MG)(NYSE:MGA) share price has declined 14% since Thursday. The shares are now 42% lower than the 52-week high of $74.

Linamar Corporation's (TSX:LNR) share price has declined about 16% since Thursday. The shares are now about 47% lower than the 52-week high of about $83.

Before you decide if you want to invest in these companies, let's take a look at their businesses and valuations.

The businesses

Magna has roughly 300 manufacturing operations and about 90 product development, engineering**,** and sales centres in 29 countries. The auto parts supplier produces the body, chassis, exterior, seating, powertrain, electronic, vision, closure and roof systems and modules. It also does complete vehicle engineering and contract manufacturing.

Linamar's history goes as far back as 1966. Fast forward to today and it has about 56 manufacturing locations, six research and development centres, and 15 sales offices in 17 countries in North and South America, Europe, and Asia.

The auto parts supplier consists of two operating segments: the Powertrain/Driveline segment and the Industrial segment, which are further divided into four operating groups–Machining and Assembly, Light Metal Casting, Forging, and Skyjack.

Revenue segmentation

In 2015 Magna earned 59.2% of its revenues from North America, 34.6% from Europe, and 7.6% from Asia and other parts of the world.

In 2015 Linamar generated 52.3% of its revenues from Canada, 23.4% from Europe, 11.6% from the United States, 7% from Mexico, and 5.7% from Asia Pacific.

Both Magna and Linamar earns a meaningful portion of their revenues from Europe. The Brexit adds more uncertainty to an investment in both companies, and that's why they have sold off.

Valuation

Magna has a market cap of $16.2 billion, which is more than six times the size of Linamar's market cap of $2.6 billion.

Although both companies are trading close to $44 per share, Magna trades at a multiple of seven. Comparatively, in the last recession it traded as low as at a multiple of eight.

Linamar trades at a multiple of 6.3, and in the last recession it traded as low as a multiple of 3.2. So, Linamar is cheaper than Magna.

Based on their normal multiples, Magna can trade at about $64 per share and Linamar can trade at about $90 per share. This means that Magna trades at a discount of 31% and Linamar trades at a discount of 51%. However, given the uncertainty surrounding the situation, investors should factor in say, +/-20%, to the fair-value estimations.

Conclusion

Magna and Linamar's share prices were dragged down 14% and 16%, respectively, due to the Brexit because both companies have a meaningful portion of their businesses in Europe.

Linamar is priced at a cheaper multiple than Magna and therefore has a bigger upside potential. However, Magna pays a bigger dividend yield of close to 3%, while Linamar's yield is less than 1%.

If you're looking to invest in the auto parts suppliers, now is not a bad time to consider doing so. However, you should have at least a three- to five-year investment horizon.

CATEGORY

1. Dividend Stocks
2. Investing

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1. Editor's Choice

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2. TSX:LNR (Linamar Corporation)
3. TSX:MG (Magna International Inc.)

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kayng