Magna International Inc. Looks Like a Value Trap

Description

Magna International Inc. (TSX:MG)(NYSE:MGA) is a Canadian auto parts maker which also assembles cars under contract from various motor vehicle manufacturers. The stock has struggled to rebound for quite some time now and is now down 22% from its high in the summer of 2015.

The company recently reported underwhelming Q4 2016 earnings results; the company missed analyst expectations thanks to rising costs. Vehicle assembly sales in Q4 were down a whopping 30% to US$439 million. I believe the 4.68% drop in the stock was warranted, and it's likely that we could see further downside from here.

The management team also warned that the rise in global protectionism may have an impact on results, and U.S. border taxes put forth by President Trump would result in further downside for the auto sector. There's no question that the stock is cheap at current levels, but is it too risky to own considering the number of headwinds the company will be facing?

Magna is one of the largest automotive suppliers in the world with 285 manufacturing operations and 83 product development, engineering, and sales centres. The company is in a globalized industry that is dependent on open borders. CEO Don Walker stated, "any proposed border adjustment tax would be negative," but he comforted investors by saying, "it's too early to tell what the Trump administration will do."

President Trump wants to bring manufacturing back to the U.S. in the hopes of strengthening the American economy. A border tax would be absolutely detrimental to a company like Magna, which exports a huge amount of raw materials to the U.S. I believe President Trump will be true to his word and will eventually implement a border tax that will hurt the long-term profitability of Canadian auto part makers such as Magna.

Sure, it's "too early" to tell what the Trump administration will do, but I believe the chance of a border tax is becoming increasingly likely, and the stock could face some serious downside later in the year.

The stock appears to be dirt cheap at current levels with an 8.43 price-to-earnings multiple, a 1.7 price-to-book multiple, and a 6.4 price-to-cash flow multiple, all of which are lower than the company's fiveyear historical average multiples of 10.8, 1.8, and 7.8, respectively. The stock also pays a 2.3% dividend yield, which is higher than it normally is at 1.8%.

I would avoid the stock because it looks like a value trap right now, especially considering the implications if a border tax is implemented. The amount of risk associated with an investment in Magna has been raised substantially since Trump’s presidential victory. I would strongly recommend looking elsewhere for value, as Magna could continue to be a laggard for the rest of 2017.

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