Linamar Corporation Boosts its Dividend by 20%

Description

The market is hard to please. Despite coming out with another record year, **Linamar Corporation's** (TSX:LNR) shares fell as much as 4% on Thursday.

With the fourth-quarter results, Linamar has experienced 22 consecutive quarters of double-digit operating earnings growth. That comes out to a length of 5.5 years — that's no small feat.

Here's what it accomplished last year.

Recent results

In 2016, Linamar increased its sales by 16% to $6 billion and increased its operating earnings by 17% to almost $697 million.

This resulted in 20% growth in its net earnings and earnings per share to $522 million and $7.92, respectively. Its net margin was 8.7% for the year, which was an improvement from 2015.

The double-digit top- and bottom-line growth were driven by its Powertrain/Driveline segment achieving operating earnings growth of 25% to $551.6 million on sales growth of 19%.

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Strong balance sheet and dividend hike

The company has been paying down its debt; its net debt to EBITDA went from about 1.5 in the first quarter to one by the end of the fourth quarter, which was faster than management's expectations.

Linamar has one of the strongest balance sheets in its industry. The growth experienced by the company and the management's confidence in its cash flow generation allowed the company to boost its dividend by 20%.

With this increase and the recent stock price of about $59.70 per share, Linamar's yield comes out to 0.8%. This is not enough to encourage dividend buyers who can easily get yields of 3-5% with growing dividends from other Canadian dividend stocks.

Perhaps Linamar can still make a good investment for value investors.

Valuation, outlook, and expected returns

The company trades at a multiple of 7.6, which seems cheap for the double-digit growth the company has been experiencing.

However, there may be a good reason for its cheap multiple. The management sees its target markets staying flat or having moderate growth this year.

The analyst consensus, across 11 analysts, expects Linamar to grow its earnings per share by 8.6-9.4% per year for the next three to five years.

Assuming Linamar trades between a multiple of 7.5 to nine, it can still deliver annualized returns of 7-15% in three years or 8-12% in five years.

Profitability

Linamar has generated good returns on equity (ROE) of at least 10% every year since 2010 and about 20% since 2013. This shows management is a good capital allocator.

With management expecting to invest 8-10% of sales back into the business, the company could continue to generate good ROE for shareholders.

Linamar's net margin was 8.4% in the fourth quarter, and the company expects to continue to maintain strong margins of 8-8.5% this year.

Investor takeaway

Even though Linamar has been doing fine, with the negative sentiment surrounding the auto parts industry, the company could continue to be punished and trade at a compressed multiple.

That said, even if sentiment doesn't change, and if Linamar experiences 8.6-9.4% growth, it can still deliver annualized returns of about 7-15% over three to five years.

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