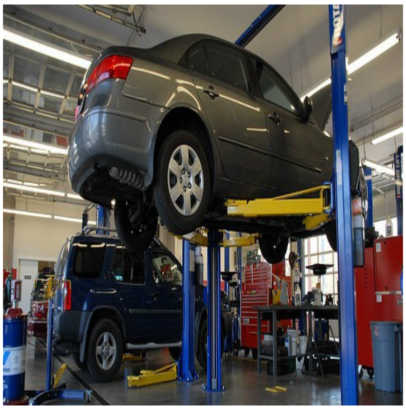

Should Investors in Magna International Inc. Be Nervous About Auto Sales and Production?

Description

On August 11, **Magna International Inc.** (TSX:MG)(NYSE:MGA) released its second-quarter results for 2017. Magna International is a Canadian automotive parts supplier. The company reported record second-quarter sales of $9.68 billion — up 3% from Q2 2016. This was achieved in spite of light-vehicle production declining in North America by 3% and in Europe by 1%. Net income was posted at $561 million representing 1% growth from the second quarter of 2016.

The board of directors declared a quarterly dividend of $0.275 per share, representing a 2% dividend yield. As of close on August 16, the stock has grown 8.64% in 2017 and 16% year over year.

Auto sales and production a mixed bag

United States auto sales declined for the fifth straight month in July as car makers reported the decline in low-margin sales to daily rental fleets. U.S. car and light truck sales fell 7% from the same period in 2016. By contrast, European sales have improved for three straight years, and Canadian auto dealers reported a record 182,000 vehicle sales in July. This represented a 4.9% increase from July 2016. Canadians continue to up their spending on vehicles in recent years, and in 2017, booming job numbers and marginal wage increases may be contributing factors.

As mentioned previously, North America has experienced a decline in auto production, and it has become a key issue in the NAFTA negotiations between the United States, Mexico, and Canada. The U.S. will look to implement America-made quotas as part of the fulfillment of the Trump administration's protectionist "America-First" policies.

There has also been growing concern about the general state of the auto industry and whether or not an auto loan bubble has formed in the North American market. For example, car loans have climbed to the largest share of U.S. household liabilities in 14 years. In Canada, auto-lending is one of the fastest-growing segments of the Canadian credit market. In 2015, the biggest growth in financing was seen in the subprime and near-prime credit tiers.

Should you buy Magna International?

NAFTA negotiations may make investors nervous about companies linked to the automotive industry in Canada, but that should not necessarily be the case. Intensified competition between economic blocks could have a positive effect for production. Canadian officials have jumped on the economic nationalist bandwagon and have called for more manufacturing to be moved north after a prolonged exodus since the 1990s.

Consumer response to higher interest rates may also give investors some anxiety when it comes to Magna International. The U.S., Canada, and European countries have claimed they are committed to normalizing interest rates, though at a tepid pace. Cheap credit has been a key driver in boosting auto sales since the 2008-2009 crisis.

Even after record earnings, I would not recommend Magna International at this time. NAFTA negotiations aside, there is simply too much uncertainty around the interest rate environment that could spark major volatility in sales in the long term.

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