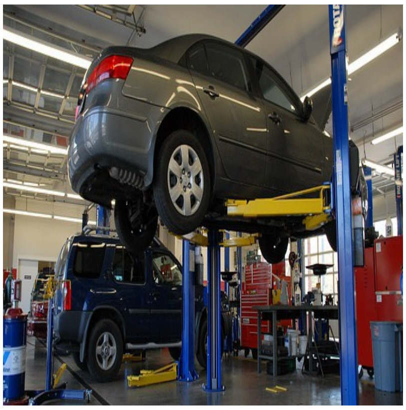

Is Linamar Corporation’s Stock a Buy or Sell After Getting Whacked?

Description

Sometimes stocks get knocked down because they deserve it.

A good example would be Snapchat’s owner, **Snap Inc.** (NASDAQ:SNAP), whose stock lost almost 17% November 8 on extremely disappointing earnings.

Then there are times where you’re left shaking your head, unable to explain the reasons behind a double-digit decline.

To me, **Linamar Corporation’s** (TSX:LNR) big slide — down 14% in November 8 trading due to questionable earnings — fits into the latter category. They might not have been stellar, but I’m not sure a double-digit haircut was called for either.

Here’s why.

Falling profits

According to the *Wall Street Journal*, analysts were expecting Linamar to deliver $1.83 in earnings per share in the third quarter ended September 30. The company delivered $1.62 per share or 14% below Q3 2016’s EPS of $1.86 and 11% shy of consensus earnings.

No wonder share have dropped so massively. There’s only one problem: the $1.83 estimate excludes one-time items and the impact of foreign exchange. In Linamar’s press release, it states that net earnings per share before those two items increased 9.4%, which would mean the non-GAAP Q3 2017 EPS number is $2.03, not $1.62.

I’ve yet to listen to the earnings call or read the transcript, but it would have been nice for the company to include the numbers from the financial statement to get to the 9.4% increase. Perhaps they will provide them at a later date.

In the meantime, it does little to reassure investors that, on a like-for-like basis, the earnings are still growing. Ultimately, yes, GAAP is the only number that counts, and it’s down 14% year over year in this instance, but Linamar's not doing itself any favours by claiming victory and then leaving out the details.

This omission has me questioning my support of its stock — something I've given on several occasions over the last year, including October 2016 and as recently as November 6.

The bigger issue

Quite rightly, Canadian investors are worried that President Trump is going to scrap NAFTA and leave Canadian auto parts companies on the outside looking in when it comes to supplying U.S. vehicle manufacturers.

"Buy American" has Linamar shareholders on pins and needles, and the company's latest report shows just how worried people are.

However, CEO Linda Hasenfratz doesn't seem concerned about some of the near-term issues Linamar faced during the quarter.

"We have had another strong quarter at Linamar despite soft North American vehicle markets," Hasenfratz stated in its Q3 2017 earnings release. "Launches are driving sales up in the Powertrain/Driveline segment to more than offset a down North American market and earnings will of course follow. We continue to generate cash to position ourselves positively for future growth and continue to see new business wins at a blistering pace."

In Hasenfratz's opinion, it's business as usual.

The reality is that if Trump withdraws America from NAFTA, the rules of NAFTA will still apply because the NAFTA Implementation Act can't be revoked without the approval of Congress. As a result, the trade rules under NAFTA wouldn't go away just because Trump wants them to.

That said, Linamar and the rest of the Canadian auto parts companies are looking to Europe and elsewhere to replace revenues that might be lost years from now once the U.S. figures out its game plan.

Is Linamar stock a buy or a sell?

If you look at Linamar's content per vehicle in dollars, all three regions of North America, Europe, and Asia saw strong increases during the third quarter.

There might be some question marks from the report, but the big one-day drop in its stock price provides a buying opportunity that, five years from now, you'll be glad you took it.

CATEGORY

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2. TSX:LNR (Linamar Corporation)

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