Should Linamar Corporation or Magna International Inc. Be Worried About NAFTA?

Description

NAFTA negotiators convened for an informal meeting in Washington in the second week of December, as talks appear to be improving somewhat after difficult summer and fall sessions. Demands from the U.S. side in recent meetings perturbed officials from Canada and Mexico. One of the stickiest points was the U.S.'s demand to up North American auto content from 62.5% to 85%, with a 50% content requirement for U.S. auto parts.

In a late October article, I'd covered why investors should be watching the auto industry closely in light of ongoing negotiations and a record auto sales year in Canada.

Linamar Corporation (TSX:LNR), which is the second-largest automobile parts manufacturer in Canada, has been vocal about its opposition to a dramatic restructuring of NAFTA. In November, I'd discussed a recent report from **Bank of Montreal** that detailed how disruptive the termination of NAFTA could be for the auto industry.

CEO Linda Hasenfratz has also argued that a push for more protectionism would have little impact on an auto industry that is seeing its biggest growth internationally. The move to increase U.S. content could be particularly damaging to Linamar if NAFTA is restructured in such a way. Less than 30% of Linamar auto manufacturing content comes from the U.S.

On December 14, Linamar announced that it would acquire harvesting specialist the MacDon Group of Companies. Linamar jumped 10% when trading opened following the news. Linamar aims to improve its agricultural business while diversifying end markets. Hasenfratz said that Linamar was looking to diversify out of the auto sector after the deal was announced.

Linamar released its third-quarter results on November 7. Sales increased 6.5%, while net earnings dipped to $107.3 million from $122.2 million in the prior year. In spite of a year of increased anxiety for auto manufacturers, Linamar stock has climbed 27% in 2017.

Magna International Inc. (TSX:MG)(NYSE:MGA) is an Aurora-based global automotive supplier. The company recently announced plans to expand its light vehicle manufacturing plant in Alabama. This was used as an example by Canadian officials in negotiations with state leaders in demonstrating Canadian investment in the U.S. Magna International stock has increased 26% in 2017 as of close on December 18.

Magna International has just under 50% of its plants and equipment located in the United States. The company appears to be safeguarded from any severe blowback in the event that the content proposition were to go forward. The company released its third-quarter results on November 9. It reported record sales of $9.5 billion, which represented a 7% increase year over year.

Does either company need to worry?

We have already gone over why Magna International is in a reasonably safe position if such a content requirement were to be included in a renegotiation agreement. However, Linamar CEO Linda Hasenfratz was skeptical, to put it mildly, that Mexico or Canada would agree to any such stipulation. Comments from officials appear to confirm the unlikelihood of this U.S. demand coming to fruition.

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Date
2025/08/25
Date Created
2017/12/19
Author
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