

Trade War Talk Weighs on Magna (TSX:MG): Should You Buy the Stock?

Description

A whopping 20%—the textbook definition of a bear market. That's how much shareholders of the automotive parts and systems maker **Magna International** ([TSX:MG](#))([NYSE:MGA](#)) have lost since June 16, as the stock sank to \$68.62 on Friday. Even on Aug. 9 when the company unveiled a surge of 15% in earnings per share to a record US\$1.67, shareholders couldn't catch a break. And they have Trump to blame.

While the U.S. president says he's the main force behind the rally in U.S. stocks because of his "America first" policy, he's been accused of trampling on the shared economic interests of the nation's closest allies. Heck, he's even struck a free-trade deal with Mexico before Canada as the 24-year-old, three-nation NAFTA agreement looks increasingly doomed.

Trump the [protectionist](#) is not only imposing unilateral tariffs on trade partners, but he's also accusing some of America's most reliable allies of currency manipulation. If trade wars are bad for business, they're even worse for companies that have production facilities across the globe, generating sales in a multitude of currencies and sourcing materials from five continents.

Geographical diversification vs global co.

That's why Magna's stock has been battered. Less than US\$7 billion of its aggregate US\$39 billion revenue last year was generated in Canada, with roughly US\$13 billion of shipments to U.S. manufacturers—mainly the Big Three automakers—and about US\$10 billion of European sales. The company, which employs 168,000 people, says it's "one of the largest automotive suppliers with 335 manufacturing operations and 96 product development, engineering and sales centers in 28 countries."

So, does the stock encompass any opportunities for value investors? First off, that June 16 level of \$86.14 was an all-time high, so one could make the case for the stock getting ahead of itself. The stock on Friday was trading at 7.82 times last year's earnings. Magna's U.S. competitor **Delphi Technologies** has a trailing P/E of 7.25 times. In Europe, the likes of **Valeo** and **Visteon Corp.** are exchanged at 10.9 and 17.04 times, respectively.

At \$68.62 a share last Friday, I'd wait a bit before getting in on the action. If the shares dip an additional 34% below the level touched on July 2, 2016, of \$45.32, it would break a support that will send the stock sinking to a four-and-a-half-year low. The situation probably won't deteriorate that much, though. However, I'd be looking to place a limit order of \$55.

To be sure, Magna did slash on Aug. 8 its full-year earnings guidance by US\$100 million to a range of US\$2.3-2.5 billion, citing not only protectionism, but also the strong dollar and headwinds at its transmission JV.

Earnings, buybacks going strong

At the other end of the spectrum, what the Aurora-based company has going for it is its product and geographic diversification combined with management's aggressive stock-repurchase plan.

While the manufacturer of products ranging from powertrains and lightings to seating systems ships goods to the four corners of the globe, it also has plants in many countries. In management textbooks, the strategy is referred to as "operational hedge," meaning that revenue denominated in various currencies is partially matched by production expenses in different countries. But does that mean that global companies stand to lose the least in downturns because of their diversification?

So far, the team in charge headed by Don Walker has consistently beaten market growth, with the 7% increase in sales last year outpacing the 2% expansion in global light vehicle production. I think there are plenty of reasons to believe this trend will continue. Magna reached a deal in June with China's **BJEV** to build an electric vehicles plant in one of the world's fastest-growing regions.

And let's not forget about the company's ambitious stock-buyback program, which has significantly contributed to boosting share prices. Of the US\$1.67 billion returned to shareholders last year, only US\$400 million were dividends as dilution decreased, boosting earnings per share 14% year on year to US\$5.96 after net income climbed to US\$2.21 billion.

The pace seems to be accelerating in 2018, with a payout of US\$233 million in the six months through June on earnings of US\$1.29 billion, and buybacks of 13.5 million shares for a US\$832 million consideration.

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