What if NAFTA Falls Apart? Should I Keep My Automotive Stocks?

Description

For years now, investors have been worried that the auto sector is at its peak. Now, we have the specter of NAFTA to worry about, further clouding the future of the automotive industry. Combine those fears with a slowing China and other geopolitical worries, and it is more than enough to keep auto investors quaking in their boots.

There are a couple of factors you should take into account before deciding whether or not you should hold on to auto stocks in anticipation of a slowdown in the auto sector or a major impact from NAFTA disintegration. The first most important fact you should be establishing is whether these businesses are solid businesses that you should be investing in at all.

Two businesses, **Magna** (TSX:MG)(NYSE:MGA) and **Linamar** (TSX:LNR) are two auto sector companies that are worth looking into to see if they are solid enough companies to invest in regardless of the political situation.

Magna

Magna’s share price has fallen significantly from its recent highs, making the price more attractive as an entry point. Besides being a major auto parts maker, the company has also entered many strategic partnerships to become involved in the self-driving car space. Magna operates all over the world providing investors with a degree of diversification.

The company’s dividend also should comfort investors since it is now around 2% and growing. Magna has been very consistent at raising its dividend for several years.

Linamar

As is the case with Magna and the rest of the auto sector stocks, Linamar's share price has come off quite a lot over the past couple of months. The company has a good balance sheet and pays a small dividend of just under 1% at the current price. While the dividend has not been raised in some time, it is well covered by the company's free cash flow. Its payout ratio is extremely low, in the single digits, so it will more than likely not be in any danger of being cut in a downturn.

The bottom line

But even though these businesses are well positioned and solid, well-run companies, should you hold on to those stocks if NAFTA falls through? This answer comes down to your allocation, how much of your portfolio is focused on this sector or is positioned within one particular stock. A good rule of thumb is to dedicate no more than 5% to any one stock. If the stock price does fall, you can simply continue to top up the position on a regular basis, say, on the first of every month, to keep the position at the 5% mark.

As a general rule, solid companies like Magna represent good long-term holds. These are cyclical companies, so you can almost guarantee that at some point there will be a downturn, especially since the auto cycle has already had a good run. As an investor, you simply need to decide how much of your portfolio you want to risk, continue adding during the bad times to maintain the percentage, and hold it for the long run.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:MGA (Magna International Inc.)
2. TSX:LNR (Linamar Corporation)
3. TSX:MG (Magna International Inc.)

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