Bad News Keeps Pouring in for This Auto Stock

Description

Canadian auto sales fell 2.5% year over year in March. This marks 13 straight months of year-over-year declines. In the summer of 2018, I'd warned investors about the worsening atmosphere for auto dealers.

DesRosiers Automotive Consultants said that auto sales fell to 181,800 units in March. Sales of passenger cars plunged 10% year over year, while light truck sales only moved up 0.6%. This latter segment has powered auto sales over the past two years. Softening numbers in the light truck segment is a grim sign for North American auto dealers.

Auto sales were also weak in the United States. This was true in March and in the entire first quarter. There is hope that a robust economy and a strong labour market will encourage more consumer spending. Unfortunately, that has yet to materialize for U.S. auto dealers in 2019.

AutoCanada (TSX:ACQ) is an Edmonton-based company that operates car dealerships across Canada. Shares dropped 1.72% on April 3. The stock has dropped 4.3% in 2019 so far.

In late 2018, AutoCanada had some reason to celebrate after the United States, Canada, and Mexico struck a tentative free trade agreement. The threat of a no-deal NAFTA cancellation drove anxiety in the auto sector, and with good reason. AutoCanada praised the breakthrough in its Q2 2018 report but warned of a challenging environment for the sector going forward.

AutoCanada released its fourth-quarter and full-year results for 2018 on March 14. For the full year, consolidated revenues rose 1.6% year over year to $3.15 billion. However, same-store revenue dropped by 1.9% and operating expenses jumped 11.4%. Gross profit fell 2.1% to $508 million, and gross profit as a percentage of revenue dropped to 16.1% from 16.7% in the prior year.

New vehicle sales decreased 0.7% from 2017 to 43,451. Revenue from the sale of new vehicles fell 1.4% year over year to $1.8 billion. Used vehicle sales, however, rose 16.7% to 22,622. Revenue from the sale of used vehicles increased 5.6% to $756.2 million. Parts, service, collision, and repair revenue climbed 8.4% from the previous year and Finance and Insurance dropped 0.4% from 2017.

The company conceded in its outlook that macroeconomic factors have created uncertainty for AutoCanada's business going forward. Further rate tightening will have a negative impact on borrowing expenses, which would in turn increase costs. However, a dovish turn from U.S. and Canadian central banks appears to bode well in the near term.

AutoCanada forecasts that it will deliver materially improved results in Canada, even in the face of broader headwinds for the auto sector. It has credited this improvement to the Go Forward Plan, which aims to increase the number of used vehicles its dealerships retail. Consumers in Canada have been overstretched in recent years, and a move to push more affordable used vehicles is a savvy shift in strategy.

The company has managed to overcome major headwinds in the auto sector, but broader headwinds keep me bearish on the stock. Currently, it is trading at the low end of its 52-week range. If shares dip below $10, value investors may want to entertain a discount purchase.

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