Auto Sales in Canada Fall Again: Avoid This Stock in 2019

Description

New vehicle sales in Canada fell for the 14th consecutive month in April. Automakers and industry boosters were quick to blame the weather for the slow month, but the excuse may be wearing thin for onlookers. Consumer confidence waned in Canada last month, which has spilled over into several industries.

To start the year, I discussed why things looked dim for automobile dealers. Canadian consumers are already some of the most over-leveraged in the developed world. Deteriorating consumer confidence will only put more pressure on this industry, even if the rate environment improves.

AutoCanada (TSX:ACQ) operates car dealerships across Canada. It offers both new and used vehicles, as well as spare parts, customer financing, and maintenance services. Shares of AutoCanada had dropped 3.3% in 2019 as of close on May 8. The stock had plunged 36% from the prior year.

Last month I warned investors about AutoCanada's prospects after auto sales reported a 13th consecutive retreat in March. AutoCanada had a strong finish to 2018, but broader headwinds have stoked negative sentiment. The company released its first-quarter results for fiscal 2019 on May 2.

Total revenue at AutoCanada climbed 19.2% year over year to $739.4 million. New vehicle retail sales jumped 20.1% year-over-year to 8,002. Revenue from the sale of new retail and fleet vehicles increased 18% to $399 million. Used retail vehicle sales surged 24.8% year over year to 5,650. Used vehicle sales accounted for just over a quarter of AutoCanada's total revenue in Q1 2019. AutoCanada's total parts, service, and collision repair and finance and insurance revenue also posted over 20% growth.

Unfortunately, AutoCanada's aggressive Go Forward Plan has been costly. Even with the big jump in total revenue, the company posted a $4.1 million loss in the first quarter. Operating expenses surged 28.2% to $122.8 million, largely offsetting the gains it has made in its segments. The addition of US operations operating expenses resulted in a $21 million tab. Total operating expenses exceeded gross profit by $7.2 million.

AutoCanada's forward-looking statement did not inspire confidence. The company projects that macroeconomic factors will continue to create uncertainty going forward. This includes a fear of future rate tightening. Central banks in the U.S. and Canada have pressed the pause button so far in 2019, but there is no guarantee that hikes will not recommence later this year or in 2020.

More concerning is the trajectory for the auto industry in North America. Sales of new vehicles are trending downwards, and AutoCanada expects a continued decline in volume for the rest of 2019. Slowing growth in Canada will add to these concerns. The economy shrank in the month of February, it appears Canada will struggle to meet a 1.5% growth target for the full year, which doesn't bode well for automobile dealers who rely on consumer strength.

AutoCanada declared a quarterly dividend of $0.10 per share in the first quarter, which represents a 3.6% yield. The slump in its share price make it an unviable target for income investors.

There is too much working against AutoCanada to consider adding it this spring.

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