Tuesday’s Earnings Recap: North American Auto Production Soars

Description

Martinrea International (TSX:MRE) reported earnings of $0.66 per share for Q2 2019 before market open on Tuesday. The company also announced positive free cash flow and a substantial reduction in debt. The higher free cash flows and reduced debt indicate that the stock price may appreciate in the next year, but investors shouldn’t bet on that outcome.

Undoubtedly, there are more profitable opportunities on the Toronto Stock Exchange than Martinrea. Although the stock’s price performance is relatively predictable, its shares only offer a dividend yield of 1.8%. Furthermore, trade tensions put Martinrea shareholders in a precarious position.

Martinrea International

Founded in 2001, Martinrea International is one of Canada’s most successful automotive engineering corporations. Significant customers of Martinrea include top North American brands such as **GM,** Chevy, and **Ford**. Also, the company operates manufacturing facilities in Mexico, Brazil, and Spain.

In the past 20 years, Martinrea has become the second-largest North American metal manufacturer in revenue terms. Moreover, the company employs 15,000 people and operates over nine million square feet of manufacturing space worldwide.

Martinrea lands new contracts

Honda and **Nissan** will employ Martinrea in the assembly of lightweight structures in 2021. These contracts are worth approximately $50 million in annual revenue. Total sales for the second quarter amounted to nearly $900 million. Martinrea expects record-breaking third-quarter sales of $860 million.

Sales in the North American segment outperformed Europe and the rest of the world. For the six months ending June 30, North American sales increased 8.5% while European and rest of the world sales decreased by 4.9% and 27.5%, respectively. The company cited lower production volume on key vehicle models such as the Jaguar Land Rover as the cause of the poor sales performance.

New NAFTA offers benefits as E.U. trade slows

Rob Wildeboer, the executive chairman of Martinrea, made comments regarding the United States-Mexico-Canada Agreement. Martinrea believes that the new trade agreement will bring many benefits to the automotive engineering sector.

Nonetheless, U.S. president Donald Trump's trade war may be blowing back on the Canadian automotive sector. Lower OEM production volumes in China led to impairment charges of $18.5 million. Impairment charges result when expected future cash flows for assets fall below the book value of the asset.

The impairment charge suggests that trade tensions between China and the United States will reduce cash flows from assets in China. Still, Wildeboer seemed optimistic about the trade conflict in his earnings comments: "… The trade and tariff issues for North America are moving in the right direction."

Foolish takeaway

Investors dedicated to North American automotive manufacturing could not do better than Martinrea. The company's return on equity is about three times the average for the Canadian automotive suppliers. Also, foreshadowing positive future performance, retained earnings increased by 50% in 2018 — the highest in the industry.

However, Tax-Free Savings Account (TFSA) and Registered Retirement Savings Plan (RRSP) investors may want to look for more profitable opportunities on the TSX. A 1.8% dividend yield is far too low of a return, and capital gain expectations are a gamble, at best. U.S. trade tensions are causing extreme financial volatility — a problem for Canadian exporters like Martinrea.

Instead, investors searching for high TFSA or RRSP returns should consider shares in insurance stocks , which offer investors both high dividends and capital gains.

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