



3 Reasons to Own This Serial Acquirer

Description

You have to go all the way back to 2008 to find a down year for **Premium Brands Holdings Corp.** ([TSX:PBH](#)) — easily one the best-performing TSX stocks over the past decade.

Premium Brands saw its stock [tumble](#) more than 7% November 14 after the release of its Q3 earnings.

Investors were concerned the company's top and bottom line were slowing from the first half of the year — revenue and adjusted EPS grew by 22% and 27%, respectively, prompting some to speculate that its growth story might be broken.

I highly doubt it for these three reasons.

The serial acquirer knows how to integrate businesses

In August, I'd highlighted the reasons Premium Brands is headed to \$200. Any story centred around the Vancouver-based food company has to begin with its knack for making [acquisitions](#); it's made more than 40 since 2005 and more than 60 in its entire history.

The company's three most recent acquisitions in the U.S. cost the company \$200 million — all of them in its growing specialty foods segment. As Fool contributor Joseph Solitro mentioned November 14, part of the company's slower growth had to do with delays in shipping orders from its new 212,000-square-foot sandwich facility in Phoenix, Arizona.

Premium Brands is pushing into the sandwich market in a big way, and that's helping improve its overall profitability. In the first nine months of the year through September 30, its specialty foods segment saw adjusted EBITDA increase by 31% year over year with margins up 70 basis points to 8.9%.

Premium Brands's acquisitions not only increase revenues but profits as well, giving it a winning formula for success.

Free cash flow

The motor that runs the acquisitive vehicle is free cash flow. You can't allocate capital that you don't have. In the trailing 12 months ended September 30, the company's free cash flow was \$136 million — 12% higher than in the same 12 months a year earlier.

Acquisitions, dividends, share repurchases, debt repayment — all of these capital-allocation levers don't get pulled without free cash flow.

The case in point is dividends.

Over the trailing 12 months, Premium Brands paid out \$1.64, 12 cents higher than a year earlier, yet its payout ratio went down 40 basis points. At the same time, its long-term debt increased 40%. If a company isn't growing its free cash flow, it's not going to be able to pay down its debt, and it will become a noose around its neck.

The secret to Premium Brands's success is using its acquisitions to grow revenues, income, and, most importantly, free cash flow. It's been doing for many years without fail, and I don't see the model changing too much in the years ahead.

Valuation

It wouldn't be accurate to call PBH stock cheap, trading at 26 times its forecasted 2018 earnings of \$4.30 a share and 21 times its 2019 EPS of \$5.13. However, with earnings growing at a compound annual rate of 25% over the past five years, it would be fair to say you're buying growth at a reasonable price.

As Warren Buffett always says, "It's far better to buy a wonderful company at a fair price than a fair company at a wonderful price."

Premium Brands is a wonderful company at a fair price.

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