Here’s 1 Stock to Definitely Buy Ahead of Earnings Next Week

Description

Earnings season is ramping up here on the TSX, and this is often an opportunity to buy in anticipation of strong performance and strong stock price rallies.

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With a 24% dividend-growth rate in 2016, a 22% dividend increase in 2017, and a doubling of the share price since January 2016, **Waste Connections** (TSX:WCN)(NYSE:WCN) stock can be expected to continue to give investors the best of both worlds: income and capital appreciation.

Waste Connections is the third-largest solid waste company in North America, and with size and a clean balance sheet on its side, the company is well positioned to continue to return cash to shareholders and pursue its goal of consolidating its fragmented industry through acquisitions.

Year to date, the stock is up 6.6%, but since the beginning of September it has fallen 7.9%.

Let’s take a look at why Waste Connections stock is a good buy ahead of its earnings results announcement on October 29.

Continuing to beat expectations

The company has handily beat EPS expectations in the last few years, and 2018 is no different.

In the second quarter of 2018, EPS came in at $0.65 versus expectations of $0.63, and in the first quarter of 2018 EPS came in at $0.56 versus expectations of $0.55.

And although valuation on this stock is not cheap, trading at 39 times this year’s expected earnings, the fact that the company is generating ample cash flow, is consistently beating expectations, and operates in a highly fragmented market that is ripe for consolidation serve to justify this valuation in my mind.

Free cash flow machine

Revenue increased 5.5% in the latest quarter, the second quarter of 2018. EBITDA increased 5.8%

and free cash flow increased 61.6%.

The company's adjusted free cash flow divided by revenue (free cash flow margin) was 13.3%.

The free cash flow margin of 13.3% (6.4% including acquisition spending) is a clear sign that the financial health of the company is excellent, as the more that the company can transform its revenue into cash, the better.

In fact, the company has been achieving an impressive free cash flow margin for years now. In 2015 and 2016, the ratio was just above 16%, and in 2017 it was just over 15%.

Balance sheet improvement

With the acquisition of Progressive Waste Solutions, Waste Connections assumed plenty of debt, and as of December 2016 it had a debt/EBITDA ratio of three times.

By December 2017, this had already come down to 2.7 times, and it still does not worry me because the company's cash flow generation is strong.

As of the latest quarter, the debt/EBITDA ratio improved even more and now stands at 2.4 times.

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In summary, Waste Connections is well positioned to continue along this path of shareholder value creation. It is a solid, well-run company that is poised to continue to do well even in a weak economy due to the defensive nature of its business.

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