VCA Antech Inc.

	Ticker: WOOF	Current Price: $31.26
	Recommendation: Sell	Target Price: $25.40
Sector: Healthcare	Analyst: Fred Rockwell	Date: April 26, 2014

Recommendation Summary

VCA Antech (WOOF) is treading water in a market that is growing and faces the risk of impairment to its $1.3B goodwill asset. I predict slower top-line growth and operating margin/multiple compression in 2014 as volumes continue to fall. Stock price has been outpacing the general market multiple expansion by 31% bolstered by a change in accounting policy, and an announced share repurchase plan in 2013. Amortization expenses no longer hit the income statement. 1-year price target of $25.40 as earnings underperform estimates and multiple shrinks.

Company Overview

WOOF operates in three complimentary segments; veterinary hospitals (77% Sales), marketing (6% Sales), and laboratories (17% Sales). The company is a roll-up, continually purchasing vet hospitals at between 5-7x EBITDA. It has 609 vet hospitals and 56 labs.

Investment Thesis

The company is losing market share in its hospital business. They had modest growth in same store sales (SSS) of 1.1% in 2013 but only after closing a record number of hospitals (3%) and increasing prices. Total customer visits declined by 2.3%. At the same Banfield animal hospitals, generally located in PetSmart stores, had SSS growth of 10%. American Veterinary Medical Association studies indicate that vet visits in the U.S. increased by 2.6% between 2001 and 2011, during this time patient volume declined by more than 20% at WOOF. The company's only organic growth has come from price increases, which are not sustainable. This problem is compounded when the company bakes growth into acquisition prices. Goodwill impairment in the hospital business is a distinct possibility. WOOF recorded impairment of $124M in 2012 and $21M in 2011 in other segments. Goodwill in the hospital business narrowly passed impairment tests in 2011. Higher prices can only support dropping volumes and compressed margins for so long. The Lab business has performed well but it does not invest in point of contact diagnostics, which is a growth space. This and the fact that many lab consumers are turned off by WOOF's roll up strategy could open the door for IDEXX to steal share.

I believe it is more than a coincidence that in 2013 2Q when hospital OM grew for the first time in two years, intercompany revenue declined for the first time in 4 years. Another suspect management action was the change in accounting policy related to amortization that increases EPS. Management is trying to paint a rosy picture.

The risk is that WOOF could acquire NVA, a network of 225 vet hospitals, which when rumored in the past raised price. I view this occurrence as unlikely given the lack of cost synergies and high asking price of NVA, 9-10x EBITDA.

Key Statistics

Market Cap.	2.72B
Total Debt	620M
52-Week	$23.66
Range	$35.61
3mo Avg. Vol.	690K
Beta	1.54
P/E ttm	20x
EV/EBITDA ttm	9.7x
2013 Hospital % of Income	56%
2013 Lab % of Income	43%
2014 Consensus Sales Growth	5.2%
Last Reported Quarter	2014 1Q
Consensus	.42
Actual	.42