# Bio-Rad's Non-Operating Income Overstates GAAP Net Income

While analyzing Bio-Rad Laboratories' (BIO) most recent 10-K, we noticed that its non-operating income not only overstates GAAP net income but could negatively impact the firm's ability to obtain additional financing.



### How Equity Investments Impact Fundamentals

Analyst Devyn DeLange found that Bio-Rad recorded a $4.5 billion (177% of revenue) unrealized gain on the change in fair market value of equity securities in 2020. This gain was primarily due to the firm's investment in Sartorius AG. In total, the firm's Other Investments (which include Sartorius AG) make up ~73% of its total assets and ~53% of its market cap.

We remove this non-operating income when calculating Core Earnings and net operating profit after-tax (NOPAT) to provide investors more reliable measures of a firm's true profitability. After adjusting for all unusual gains/losses, Bio-Rad's Core Earnings of $293 million are much lower than GAAP net income of $3.8 billion.

We also add back the **unrealized** gains and subtract the **realized** gains on equity securities to Bio-Rad's accumulated other comprehensive income (OCI). We then subtract OCI from our invested capital calculation to better represent the actual capital on which management should generate a return. Without adjusting both the income statement and balance sheet, investors get a misleading picture of a firm's return on invested capital (ROIC) and true free cash flows. Get more details on how gains on equity securities impact OCI and invested capital here.

Beyond creating misleading GAAP net income, Bio-Rad's investment in Sartorius AG jeopardizes its ability to access capital markets. Based on the value of the firm's position in Sartorius AG, Bio-Rad might be deemed an investment company (rather than a Healthcare company) under the Investment Company Act, as noted on page 13 of its 2020 10-K. Should such classification occur, the firm notes it "might not be able to access the capital markets or otherwise obtain financing…" and "If the Company were deemed to be an investment company such determination could have a material adverse effect on our business."

### How We Treat Non-Operating Items

Non-operating items, such as Bio-Rad's unrealized gain on the change in fair market value of equity securities, are why GAAP net income and analyst earnings don't tell the whole story of a company's profitability. We adjust for all unusual items, both hidden and reported, to calculate a more accurate measure of a firm's profitability.

Without such diligence, investors could make misinformed investment decisions, and, in the case of Bio-Rad, be unaware of possible material changes to the company's financing capabilities.

Only our "novel dataset", which leverages our Robo-Analyst technology, enables investors to overcome flaws with legacy fundamental datasets to apply reliable fundamental data in their research. Core Earnings: New Data & Evidence, accepted for publication by The Journal of Financial Economics also proves the superiority of our fundamental data, Core Earnings models, and securities research.

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*Disclosure: David Trainer, Devyn DeLange, Kyle Guske II, and Matt Shuler receive no compensation to write about any specific stock, sector, style, or theme.*

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Forthcoming in The Journal of Financial Economics, a top peer-reviewed journal, Core Earnings: New Data & Evidence proves our Robo-Analyst technology overcomes material shortcomings in legacy firms' data collection processes to provide superior fundamental data, earnings models, and research. More details.

Key quotes from the paper:

- "[New Constructs'] *Total Adjustments* differs significantly from the items identified and excluded from Compustat's adjusted earnings measures. For example… 50% to 70% of the variation in *Total Adjustments* is not explained by *S&P Global's (SPGI) Adjustments* individually." – pp. 14, 1st para.

- "A final source of differences [between New Constructs' and S&P Global's data] is due to data collection oversights…we identified cases where Compustat did not collect information relating to firms' income that is useful in assessing core earnings." – pp. 16, 2nd para.

**Superior Models**

A top accounting firm features the superiority of our ROIC, NOPAT and Invested Capital research to Capital IQ & Bloomberg's in Getting ROIC Right. See the Appendix for direct comparison details.

Key quotes from the paper:

- "…an accurate calculation of ROIC requires more diligence than often occurs in some of the common, off-the-shelf ROIC calculations. Only by scouring the footnotes and the MD&A [ as New Constructs does] can investors get an accurate calculation of ROIC." – pp. 8, 5th para.

- "The majority of the difference…comes from New Constructs' machine learning approach, which leverages technology to calculate ROIC by applying accounting adjustments that may be buried deeply in the footnotes across thousands of companies." – pp. 4, 2nd para.

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Key quotes from the paper:

- "the portfolios formed following the buy recommendations of Robo-Analysts earn abnormal returns that are statistically and economically significant." – pp. 6, 3rd para.

- "Our results ultimately suggest that Robo-Analysts are a valuable, alternative information intermediary to traditional sell-side analysts." – pp. 20, 3rd para.

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