Should Investors Buy Sierra Wireless Inc. Now or Stay on the Sidelines?

Description

Sierra Wireless Inc. (TSX:SW)(NASDAQ:SWIR) is down over 15% year to date. This will definitely pique the interest of investors as they look for an attractive entry point into the stock. Let's look at this in order to determine if this is a good time to step in or if investors should stay on the sidelines.

Most recent quarter

The most recent quarter was strong, beating expectations with a 21% organic growth rate in revenue and a gross margin of 33.6% compared with 32.5% in the fourth quarter of 2013. Free cash flow generated in the quarter (excluding the effect of working capital) was $4.4 million, and cash on the balance sheet increased to $207 million.

During the quarter, the company made a $90 million cash acquisition of Sweden-based Wireless Maingate, a company with 2014 revenue of over US$19 million and EBITDA of US$6 million. Wireless Maingate provides M2M connectivity and data management services, and this acquisition represents significant progress in solidifying Sierra Wireless' device-to-cloud business. The acquisition metrics were reasonable, at 4.7 times sales and 15 times EBITDA. For comparison purposes, Sierra is trading at an EBITDA multiple of almost 30 times.

Industry fundamentals

As we know, machine to machine communication is an industry that is growing fast. It is a fragmented market that Sierra Wireless is well positioned to consolidate, as we are at the beginning of a secular trend that is here to stay.

Long term, it is reasonable to expect that most machines will be connected, providing financial, service, and lifestyle benefits to users of these machines. Infonetics Research predicts that revenue from M2M services will more than double from just under $15 billion in 2012 to $31 billion in 2017. As Sierra is now focused solely on the M2M business and currently boasts a leading market share, it stands to benefit greatly from this growth.

Expectations

There are 13 analysts covering the stock, and the consensus EPS estimate for the next quarter is $0.18 per share, which is up a lot from the $0.02 per share in the same period last year. The variation of earnings estimates is reasonable, with the low being $0.16 and the high at $0.19. Revenue guidance for 2015 is for $145 million to $149 million for a growth rate between 20-23%.

Valuation

In my view, the major caveat regarding Sierra Wireless is the fact that valuations are high. On a GAAP basis, the company has no earnings, and on an adjusted, non-GAAP basis, it is trading at a P/E of 80 times 2014 EPS and almost 60 times expected 2015 adjusted EPS. In my view, Sierra is currently priced for perfection and this can turn bad pretty quickly. While I like Sierra's fundamentals, performance, and outlook, it seems to me that investors would be wise to sit back and wait for a better entry point.

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2. Tech Stocks

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1. Editor's Choice

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