Big Money Likes This Automation Stock

Description

Automation Tooling Systems Inc. (TSX:ATA), with its $1.3 billion market cap, may be new to you, but it's not new not to Motley Fool Canada contributors. Based in Cambridge, Ontario, ATS is a global technology company that provides automatic manufacturing solutions to other businesses. There are 23 manufacturing facilities. Next year will be its 40th anniversary, and the company has traded publicly for 25 years. ATS supplies equipment to businesses across four markets: life science, transportation, energy, and consumer equipment.

Revenue is down a few percent in 2017 compared to 2016 when the company generated $1.04 billion in revenue. The company attributed earnings drop due to stock-based compensation, which went up considerably, but it is hard to see how this line item (which is small) drove earnings down. The stock price was mostly flat year to date until investors viewed ATS as undervalued, sending the stock on an 18% run from September through October. The stock blew past the 200-week moving average, around $13 per share, and now sits at $14 and change. This stock has been as high as $16 — another 11% increase if momentum stays favourable.

Like many tech companies, ATS has a high multiple compared to other sectors. It has a price-to-earnings ratio (P/E) of 39, which is more than twice the TSX average but close to normal for this company. A better indicator for ATS might be the price-to-sales ratio (P/S), since this says something about price relative to future revenue. On this metric, ATS is looking pretty solid because high sales will drive P/S down, which is what appears to be happening.

ATS behind the numbers

Orders are up. ATS customers in the life science sector appear to be driving growth, since this is where orders have surged. Examples of a life science application are automated test tube filling devices and equipment that checks for vial defects. It is easy to see how this equipment would be valuable. ATS generates good cash flows, as reflected by $287 million cash on hand.

The company appears to have a list of loyal customers since repeat customers placed 90% of the bookings. For a small-cap company, this is a good sign, but the company will need to scale things up to drive growth. One additional source of revenue is after-sales service calls, which makes sense given that the automation equipment may be highly customized and also expensive (in some cases, equipment will cost $10 million).

ATS has said it will focus on three product areas to drive growth in the future: 1) advanced linear motion systems designed to move products over small scales; 2) vision systems that improve automated material handling and feeder technologies; and 3) work on industrial internet of things (IOT) to predict equipment maintenance time frames to prevent failures. Innovation is a strong focus for this company.

In conclusion, ATS is a nice homegrown tech story that has quietly grown and is poised to continue, as automation becomes more a part of industrial activities. It is good that the business is diverse across different fields compared to more focused tech businesses that have flared and flunked in Canada. Brand recognition is, however, something ATS could work on. The new CEO, appointed in 2017, has taken the helm at a good time. Institutional investors have a large stake in this company, which is a good sign.

ATS is a company to add to your watch list.

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