Kinaxis Inc. Shares Rise +14% in 2 Days: Could This Be a Return of Share Price Growth Momentum to the Stock?

Description

Shares of **Kinaxis Inc.** (TSX:KXS) rose 14.6% in the last two trading days of last week after the tech growth firm reported some good third-quarter (Q3 2017) results on Wednesday, November 1. Investors could expect a return of share price growth momentum on the stock.

Kinaxis is one of the leading supply chain management solutions providers with its flagship software offering, the Rapid Response package, generating sustainable growth momentum and battling it out with other global powerhouses, such as the likes of **SAP SE** in Germany and JDA Software Group Inc. in the United States.

Kinaxis's stock has become very volatile after some bad news on August 8, when it tumbled 21% to hit a low of $63.66 on August 10, as investors were disappointed by a US$10 million downward revision to the company's 2017 revenue guidance and a new business strategy that threatened to slow down professional services revenue growth.

Some investor confidence might have returned to the stock after Kinaxis reported stellar Q3 2017 results and the stock rebounded significantly.

Could this be a sign of a return to share price growth momentum to Kinaxis's stock?

Possibly.

Kinaxis continues on a steady growth path after reporting a 24% growth in subscription revenue in Q3 as compared to the same period last year. Subscriptions are the main revenue growth driver going forward.

The company has adjusted its revenue growth guidance for the year by US$1 million from the US$131-133 million guidance given in August to a new range of US$132-134 million.

Most noteworthy, the company has also guided for a 22-23% subscription revenue growth for 2017, which puts the company's core revenue driver in a high growth category in the industry, potentially justifying the high 91 times trailing price-to-earnings (P/E) multiple on the stock price.

Kinaxis has recorded sequential quarter-on-quarter growth in gross margins this year, rising from 68% in the first quarter to 70% of revenue in the second quarter before hitting 71% in the third quarter. This significant profitability improvement has gone on to boost the bottom line too.

Another notable achievement for Kinaxis was in its recent cost-management performance, where selling and marketing expenses have fallen from being 27% of revenue in the third quarter of 2016 to 21% of revenue in Q3 2017.

However, I do expect selling and marketing expenses to grow this quarter and the next, since the company expenses all deal-negotiation costs in full upon the first revenue recognition for new contracts, but management seems to be upping their cost-management stamina, as depicted in the sequentially rising adjusted operating profits (adjusted EBITDA) to 59% of revenue last quarter.

Potential problem

Kinaxis has since cancelled its contract with the problematic large Asian client which caused the revenue guidance revision in August, and the matter has gone for arbitration. The client alleges breach by Kinaxis and has asserted counter claims. If Kinaxis loses the case, it may have to write off about US$2.5 million in revenue recognized before March 30, 2017.

Investor takeaway

Kinaxis's growth story continues, even as professional services revenue is shared with technical partners.

Management foresees the company realizing exponential growth going forward, as the new partners accelerate subscription revenue growth through their more privileged direct engagement with end-users.

Most interesting, the company holds no long-term debt in its capital structure, leading to a lower-risk profile. Furthermore, Kinaxis enjoys almost 100% revenue retention from its sticky multi-year client contracts, bolstering the case for sustainable revenue growth.

However, Canada segment revenue continues on sequential decline. It would be great for the company to grow in its home market.

I am expecting a sustained double-digit revenue and profitability growth momentum for Kinaxis in the long term, which may be accelerated by the new technical partners' involvement and supported by the company's elevated capital expenditures, which may total US$10-11 million this year.

However, as discussed earlier, a $100 share price may not be realized in the near term.

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