A Good Value Tech Stock for Long-Term Growth

Description

Open Text Corp. (TSX:OTEX)(NASDAQ:OTEX) stock has outperformed the NASDAQ in the long run, ending 2017 with a 20-year total return of 2,194% compared to NASDAQ's 405%.

The global enterprise information management software and cloud services company is a successful roll-up story, completing 59 acquisitions so far. More than half of those acquisitions were done in the last 10 years.

It's not easy combining businesses with various cultures and technologies while improving efficiency and profitability, but Open Text has shown that it has the ability to do just that. Most recently, the company expanded into the areas of security, Internet of Things (via the Covisint acquisition), artificial intelligence in the context of enterprise information management.

Last fiscal year, Open Text achieved nearly US$2.3 billion of revenue with 41% of the sales outside the Americas. In comparison, the total addressable market is ~US$40 billion and growing. Thus, Open Text has plenty of room to grow. Currently, it has key operations in Canada, the U.S., the U.K., Germany, France, India, Philippines, Australia, Japan, and Brazil.

Profitability

Open Text has been focused on expanding its annual recurring revenue (ARR), adjusted operating margin, and operating cash flow. Its recurring revenue consists of cloud services, subscriptions revenue, and customer support revenue. It is a high-quality form of revenue because of its recurring nature.

In the second quarter of fiscal 2018, Open Text's ARR made up 70% of its total revenue. In the past 10 fiscal years, Open Text expanded its adjusted operating margin from 22% to 32%. In the same period, its operating cash flow per share increased at a compound annual growth rate of nearly 12%.

Open Text can also further automate its operations, which should help lower costs and improve efficiency. In the last few years, Open Text has normally maintained returns on assets of ~6%, returns on equity of ~13-15%, and returns on invested capital of +7%.

Dividend and valuation

Open Text began paying a dividend in 2013, increasing it every year since 2014. Its three-year dividend growth rate is 15.3%.

At US$35.30 per share, Open Text trades at a multiple of ~14.1. Analysts believe the company can continue growing at a double-digit rate for the next three to five years. Open Text is therefore a good value today. With a payout ratio of ~20% this year, it can also grow its dividend at a nice clip.

Investor takeaway

Open Text can deliver a double-digit rate of return for the next three to five years. However, it will largely depend on the success of its acquisitions and integrations, which are the company's largest growth driver. To put it in perspective, in the past five years, Open Text spent US$1 billion in research and development and US$4.7 billion in acquisitions.

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Author
kayng