Kinaxis Inc. (TSX:KXS) Stock Couldn’t Resist a Good Quarter Report

Description

The emerging supply chain management software provider**, Kinaxis Inc.** (TSX:KXS) is one tech stock of choice in the Canadian investment space as the firm continues to churn out ever improving numbers, this time with an added edge from new accounting rules. The stock price has continued to respond positively, up 20% so far this year.

The company’s second quarter results were positive from several angles.

Strong revenue growth

Second quarter revenue grew a good 18.65% from comparable quarter readings in 2017, and half year revenue was almost 16% higher than that of last year’s levels. The company’s revenue guidance for this year is for corporate revenues of between US$150-154 million, or US$158-163 million using the old revenue recognition model prior to IFRS 15 and 16 adoption; this is up from US$133 million last year.

Management expects growth in subscription services revenue of 23-26% year-over-year and adjusted operating earnings (adjusted EBITDA) margin of between 24-27% of revenue for the year.

I like Kinaxis’s strong revenue visibility, with most of the company’s revenue highly recurring due to a strong subscription model in which current subscription term licenses average a 7-8 year lifespan.

Blessings from new accounting policies

The recent introduction of two new accounting rules, namely International Financial Reporting Standard (IFRS) 15, which modified revenue and expense recognition policies, and IFRS 16, which dealt with accounting for leases, the company has seen some delayed expense recognition and improving operating margins.

Starting January 1, 2018, Kinaxis can now legally capitalize some of its marketing expenses, especially customer acquisition costs under IFRS 15. The company used to immediately expense these costs, but the sums can now be amortized over the life of the contract, which could generally be six years.

Further, IFRS 15 has also resulted in some aggressive revenue recognition practices from Kinaxis contracts, with earlier recognition of revenue for identifiable subscription arrangements, but the effect on quarterly revenue hasn’t been that straightforward on a quarter to quarter basis.

Due to IFRS 15 and 16 adoption this year, second-quarter revenue was 2.48% lower than it could have been without the standard, operating profit was 7% lower, net profit was 3.6% lower, but income tax expense was 14.95% lower than it would have been. However, operating margins were significantly higher due to capitalized expenses.

The impact of IFRS 15 and 16 was muted in the half year results, however, with no significant effect on revenue for the first six months of 2018, but with a significant reduction in selling and marketing expenses by 12% and a corresponding increase in operating profit by 18% for the first half the year.

Growth in operating cash flow generation

There has been a sustained growth in operating cash flows from Kinaxis' business model. Cash flow from operations grew by a staggering 23% for the second quarter as compared to the same period last year. Cash is king, and this growth in cash flow will allow Kinaxis to minimize potential for shareholder dilution from new equity issues in efforts to raise investment funds. This is a big positive for the stock.

G**eographical segment performance**

The European segment marketing efforts are showing explosive results this year as revenue from this continent has grown by 381% in the first half of 2018 as compared to 2017. The second highest growth market is the U.S., where the company recorded an 8.09% sequential revenue growth in the first six months of 2018.

Canada revenue performance remains very unimpressive, declining 24% from last year performance. The Canada segment revenue, where the company has invested 51.15% of its assets, has shrunk to just 1.26% of total revenue in the first half of the year, while U.S.A. revenue has risen to constitute 81.5% of corporate top-line during the period.

Kinaxis could do better in its home country.

Investor takeaway

That Asian customer that caused all the stock price agony last year shouldn't be forgotten just yet, however. The company still believes the $2.5 million collectable under a disputed contract is still collectable, and the matter is under a binding arbitration. The customer has also made counterclaims, but management has not made any provision for liabilities should Kinaxis lose the case. This is one of those snags that investors just need to shrug off.

Otherwise, the company's high tech growth engine is all fired up, and the stock is all set to hit that $100 mark this year.

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Author
brianparadza