After Falling Off a Cliff, This Stock Has Massive Upside

Description

Kinaxis (TSX:KXS), the $1.7 billion market capitalization tech company that has been a high flyer since its IPO in 2014, has returned more than 400% for investors over this period.

The Ottawa-based developer of cloud-based supply-chain management solutions has gained market acceptance and market share, more than doubling its revenue since 2014 and achieving a compound annual growth rate in revenue of 22% over this period.

In the last year, Kinaxis stock has been volatile, but is pretty much flat, despite continued double-digit revenue growth, continued free cash flow generation, and a strong balance sheet.

So, what happened to precipitate a free fall?

Well, the latest quarter was disappointing, and Kinaxis stock plummeted almost 20% off these results. It didn't help that the stock was trading at almost 100 times this year's earnings, but as a growth stock, and in the context of the risk-taking market we were in this year, these things are to be expected, as investors bid up the stock price.

But now sentiment is decidedly shifting.

And this — along with results that were disappointing — has worked to bring the stock down to more reasonable levels. So, valuations are better, albeit still high, at roughly 65 times this year's expected EPS and 51 times next year's consensus expected EPS.

And the question is whether these estimates are on the way down or on the way up.

The recent miss was apparently due to a timing issue, as certain deals that were supposed to close in the third quarter didn't make the deadline. And after a prolonged period where the company was beating expectations, investors are now worried about whether the company will even meet expectations.

At this point, it would be helpful to take a step back and look at the big picture.

Kinaxis is a high-margin, profitable, cash flow-generating company that has proven itself to be a player to be reckoned with in the tech industry.

With EBITDA margins of almost 30%, a solid history of free cash flow generation, all while investing for growth, and a strong low-debt balance sheet, the stock is a fundamentally solid one for investors.

Free cash flow was slightly positive this last quarter, but was $4.7 million in the second quarter, $5.7 million in the first quarter, and is expected to recover in the fourth quarter.

I think that with Kinaxis, investors would be well advised to stay on the sidelines for now, as stock prices in the market adjust to the new reality of increased risk aversion, thereby bringing down those growth stocks that are especially highly valued, like Kinaxis.

But the long-term outlook is still favourable, so I would monitor the stock and pick my entry point in preparation to add it to my portfolio.

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