



A Dividend Stock With High Growth? Absolutely!

Description

Vancouver-based **Absolute Software** (TSX:ABT) is my clear favourite in a market I think is deeply underappreciated: cyber security.

According to a recent industry report by the **Canadian Imperial Bank of Commerce** (CIBC), cyber crime such as data hacks, fraud, malware, ransomware, copyright infringement, and unwarranted mass-surveillance could be draining \$3 trillion from the global economy every single year.

Cyber attackers are becoming increasingly sophisticated as the tools they use become cheaper and more capable. Meanwhile, the focus has turned to small and medium-sized enterprises which are more vulnerable to attack. This has sparked an arms race between cyber attackers and defenders, and the weapons are supplied by a handful of cyber security firms.

Absolute isn't the biggest or most well-known player in the cyber security field, but it does offer investors two clear advantages – a steady and growing dividend and a reasonable valuation.

At its current market price, ABT stock offers a 3.5% dividend yield. Over the past five years, the dividend yield has averaged 4%. The most recent dividend payout ratio was 155%, because the company returned all net earnings and a little bit of cash to shareholders over the past year.

Given that Absolute has a cash hoard of over \$34 million, it can fully cover the current rate of dividend for the next three years without any earnings. Meanwhile, the company's asset-light business model lets it operate without the need for any debt.

After taking a deep dive into Absolute's books, I believe the dividend is built on a solid foundation. The company's cyber security software solutions have been integrated with the systems of over 12,000 corporate clients from across the world. 95% of the income is recurring and the gross margin on each deal could be as high as 85%.

Meanwhile, the demand for cyber security tools continues to expand. Over the past few years, every high-profile data breach or cyber attack has made business leaders more paranoid. Small- and medium-sized enterprises don't recognize the necessity of these tools yet, but a significant loss or reputation damage could push them towards adoption.

According to Absolute's investor presentation, demand for its security solutions isn't just driven by business need, but also by regulations. Europe's push for greater data security, restrictions on data use in emerging markets like India, and the *Health Insurance Portability and Accountability Act* of 1996 (HIPAA) in the United States are all driving growth in Absolute's niche.

To remain at the forefront of this growing industry, Absolute is deploying a significant amount of cash towards research and development. Over the past two years, R&D costs have averaged about 20% of gross revenue.

Analysts expect the company to deliver 3% to 6% revenue growth, gross margin of 17.5%, and an average 50% earnings growth through 2020. At the current market price, the stock's price-to-earnings to growth (PEG) ratio works out to 1.12, which is fairly valued.

Bottom line

Absolute is a cash-rich security firm with a solid base of recurring revenue, steady dividends, and attractive growth prospects. Because it's still flying under the radar, investors may have the opportunity to enter at a fair price right now.

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