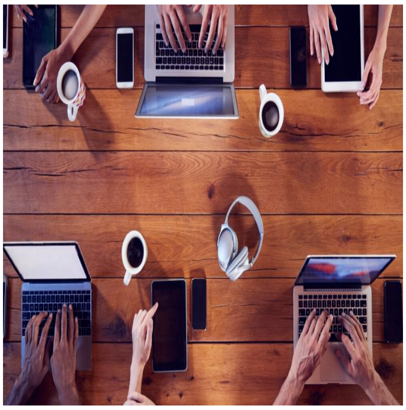

This Multibagger Tech Stock Just Corrected +40%: Is it Time to Buy?

Description

Tucows (TSX:TC)(NASDAQ:TCX) stock corrected more than 40% from the $120-per-share area. Technically, it appears to be a good time to nibble some shares, as the growth stock trades at a support level.

Delivered outsized shareholder returns

Tucows was founded in 1993. Along the way, the company made a number of acquisitions, which have proven to be great moves, as the stock has generated tremendous shareholder value over the long run.

An investment in Tucows stock in 2007 would have been nearly a 15-bagger by today! To put it in perspective, a $10,000 investment would have transformed to nearly $150,000. This equates to an annualized return of about 24%.

The business

Tucows has two business segments: Domain Services (72% of 2018 revenue) and Network Access Services (28%). The Domain Services segment has three service offerings: wholesale, retail, and portfolio.

The Network Access Services segment primarily derives revenue from selling retail mobile phones, telephony services, and high-speed internet access to individuals and small businesses.

Tucows is the second-largest domain name registrar in the world. Because domain names for websites must be renewed every year, it is a stable cash flow generator. At the end of the first quarter, it had about 25 million domains under management, which was an increase of 3.5% from a year ago.

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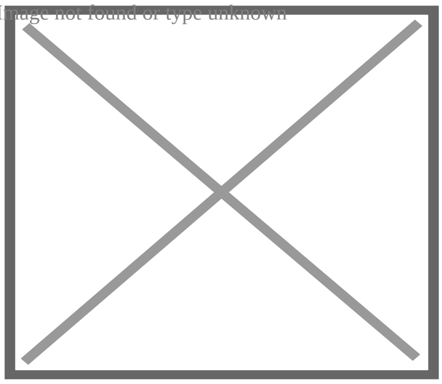

Profitability

Revenue growth is often a booster of earnings growth. Therefore, Tucows's three-year revenue growth of 26% per year to US$346 million in 2018 is encouraging to see.

In the same period, its operating income increased by about 16% per year to US$29.6 million, while its net income climbed about 15% per year to US$17.1 million. On a per-share basis, earnings climbed 16.7% per year.

One thing that's worth noting is that since 2009, Tucows has had very strong double-digit returns on equity (ROE) for every year but one year. Its five-year ROE was 35%, while its trailing 12-month (TTM) ROE was 22%. The strong track record of ROE indicates that management has allocated capital in the right places to generate excellent returns for shareholders.

The problem

The company seems to be having trouble keeping its mobile customers. Its mobile accounts under management has been on a decline every quarter since the first quarter of 2018. Specifically, from a year ago, it's down 3.2%.

The company is banking on growth from its internet service. It has been investing in fibre to improve the speed and service area of its internet service.

In the TTM, Tucows invested US$27.5 million in fibre (roughly 75% of cash flow). As a result, its internet subscribers under management has increased by 54% from a year ago.

Foolish takeaway

Tucows is investing a large portion of its cash flow in fibre. Therefore, the company's future growth heavily relies on the results of these investments. However, its internet business makes up only a small part of its business currently.

Bullish investors can nibble some shares, as analysts believe the stock should trade 21-51% higher from current levels. Cautious investors should wait for the company to improve its mobile customer retention or taper off on its fibre investments (which will indicate stronger free cash flow generation) before considering a position.

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