1 Small-Cap Tech Stock to Consider Buying for Your TFSA

Description

Supply chain solutions provider **Tecsys** (TSX:TCS) is a small-cap stock that has recently returned to double-digit organic revenue growth, while expanding internationally into new markets and generating expanded profit margins lately. Long-term growth investors should take notice early to capture the upside.

Tecsys is an enterprise supply chain management software developer with a strong healthcare niche in North America and a growing portfolio of new international retail, wholesale distribution, and logistics clients.

The company released encouraging fiscal first-quarter 2020 results on September 5, and shares rallied as investors celebrated a reported 49% year-over-year revenue growth to $24.3 million and higher profit margins for the quarter ended on July 31 this year.

Although the acquisition of OrderDynamics in November last year and a takeover of PCSYS in February 2019 significantly contributed to top line growth, the old business portfolio saw sales increase by 15% organically from a comparable quarter last year, as the company converted an early professional services bookings backlog into sales.

Thanks to the new acquisitions, TCS is growing its footprint into a global business in new geographic markets including Europe and Australia, as well as serving new industries like retail, manufacturing, and logistics. Revenue and cash flows could increasingly become less volatile with this increased diversification.

Margin expansions

Tecsys's sudden return to margin growth after weaknesses in a previous quarter deserves some celebration.

The company's quarterly gross margin expanded by 100 basis points to 48% during the quarter, up from 47% during the same period last year as services gross margins expanded.

Operating earnings grew faster than revenues too as costs remain contained.

Most noteworthy, adjusted EBITDA saw a big 272% increase when compared to the same quarter last year, and the adjusted EBITDA margin, a key measure of sustainable operating profitability, rose to 8.2% of revenue, up from 3.3% for the same quarter last year. The company recently became more profitable.

That said, the company implemented a new accounting standard called IFRS 16: Leases, during the quarter, which positively impacted the adjusted EBITDA, but if we adjust for this change, the second-quarter adjusted EBITDA margin would still be 6.99% of revenue, or double that for the first quarter. This is some positive progress if the new margins can be sustained.

More recurring revenue

As the disruptive migration from one-time licence revenues to cloud-hosted Software as a Service (SaaS) subscription-based business models gathers pace in the tech industry, sales become increasingly recurring in nature.

TCS grew its annual recurring revenue by over 40% during the past year. Higher recurring revenue means better earnings and cash flow visibility. Investors willingly pay a premium on equities with highly visible earnings.

Potential risks to consider

Revenue growth is strong, but cash flow generation has suffered after acquisitions and working capital changes. This should be temporary.

Further, financial leverage increased significantly this year, as the company borrowed to finance new acquisitions. Management is committed to paying down the debt fast, but we need to monitor progress going forward given the recent negative cash flows.

Foolish bottom line

Tecsys has reported impressive growth and margin expansions while expanding its presence into new territories and markets. More growth could be expected, as the company enjoys more business from its recession-proof healthcare sector niche, and shares could rise with further profitability growth over the next five years.

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Date
2025/09/09
Date Created
2019/09/23
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