This High-Growth Stock Is Down 25%: Should You Buy?

Description

The stock market has turned from bearish to bullish as the seasonal rally kicks in. In this turn of events, a few high-growth stocks dipped significantly for company-specific reasons. One of these high-growth stocks is **Dye & Durham** (TSX:DND), the software company that stormed the market and gave handsome returns in a year. But now the stock is down 25%. Should you buy this dip?

Many investors fear a dip because not all stocks rise from the decline. Investors should understand why the stock fell and how it impacted the company's fundamentals and long-term growth potential. For instance, **Air Canada** stock fell over 65% in March 2020 because of the pandemic. The cause of the dip impacted its fundamentals and growth.

Dye & Durham stock fell 25%

Dye & Durham is a cloud-based software offering information services and workflow to legal, government, and financial services firms. The critical nature of its services in a niche market makes the software sticky. Its clients are blue-chip firms, and top 100 accounts have an average contract of 16.6 years. This means regular and predictable cash flow.

With such a robust clientele and earnings, Dye & Durham stock surged threefold in a year since its initial public offering (IPO) in July 2020. For a company with predictable cash flows, why did the stock fell 25%?

The stock fell around 13% between July and September. That is normal for a high-growth stock because the overall market was slow at that time. Moreover, there was some insider selling. But the steep fall I am talking about came on October 7. It was from that day the stock fell almost 14%. There was significant selling activity, making the stock oversold.

Why did Dye & Durham stock fell?

This sudden sell-off came as Dye & Durham rejected a $2.8 billion buyout offer after careful consideration. It also formed a special committee to analyze the offer. The committee recommended going with the existing business strategy of growing through acquisitions rather than getting acquired.

I was expecting a similar outcome. Think logically. Why would a company in the growth phase whose stock has touched a high of $53.68 go private for a $50.5/share offer? Mawer Investment Management, who owned about a 9% stake in Dye & Durham at that time, also opposed the idea of going private.

Probably, the management firm that proposed the acquisition might have sold some or all of its shares in Dye & Durham after the latter rejected the offer. But this sell-off is temporary.

Should you buy the dip?

The dip is because of a rejected offer, which will not impact Dye & Durham's contracts. The company will continue to acquire more companies and grow its client base. Its acquisition-driven business model targets companies with a strong client base and adjusted EBITDA. In its investor presentation, the company said that the acquisitions in the pipeline have worth over $500 million in adjusted EBITDA.

It expects a fivefold growth in adjusted EBITDA from $36.7 million in fiscal 2020 to $200 million by fiscal 2022 through acquisition, integration, and operations. The company has exceeded its target adjusted EBITDA growth in the last three years (2019-2021). Even if I consider the company's target as ambitious, there is no denying the company is growing fast.

There is long-term growth potential in the stock. I don't say Dye & Durham's share will grow 200% in a year, but it can grow double-digit in the next five years. This is an opportunity to buy a high-growth stock at a significant discount.

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