This Growth Stock Rallied 20% Yesterday, But it’s Still Cheap!

Description

High inflation followed by rising interest rates triggered a selloff in growth stocks. Specifically for **Converge Technology Solutions** (TSX:CTS), as much as 63% of its value was wiped out, as the stock fell from a peak of about $13 to a trough of under $5.

The tech stock stayed briefly at the $5 level before making its way to $6. Yesterday, it surprised the market by rallying more than 20% from the previous market close price of $5.89 per share to $7.10.

The reason for the rally was simple. Converge had a blowout quarter!

Highlights for the awesome quarter

- Net revenues jumped 73% to $596.66 million versus the same quarter a year ago
- Gross profit rose 70% to $133.15 million year over year
- Adjusted EBITDA (earnings before interest, taxes, depreciation, and amortization), a cash flow proxy, increased by 80% to $39.19 million
- Adjusted EBITDA margin improved to 6.6% from 6.3%
- Net income increased by a whopping 1,039% to $11.68 million
- Net income per share rose 400% to $0.05
- Adjusted net income jumped 111% to $29.90 million
- Adjusted earnings per share (EPS) rose 75% to $0.14

The demand for Converge’s diversified tech solution offerings remains strong. Its product bookings backlog increased to roughly $507 million in the second quarter (Q2) versus the $472 million in Q1 2022, after delivering $375 million worth of Q1 product backlog in Q2. It means $410 million worth of new business came in during Q2. Its service backlog also increased to $71 million versus $45 million in Q1.

Results in the first half of the year

Results in the first half (H1) of the year shows a bigger picture. Here are some highlights:

- Net revenues jumped 75% to $1.15 billion versus H1 2021
- Gross profit rose 66% to $252.20 million year over year
- Adjusted EBITDA increased by 70% to $68.84 million
- Adjusted EBITDA margin dropped to 6.0% from 6.2%
- Net income increased by a 98% to $9.27 million
- Net income per share rose 67% to $0.05
- Adjusted net income doubled to $52.41 million
- Adjusted EPS rose 50% to $0.24

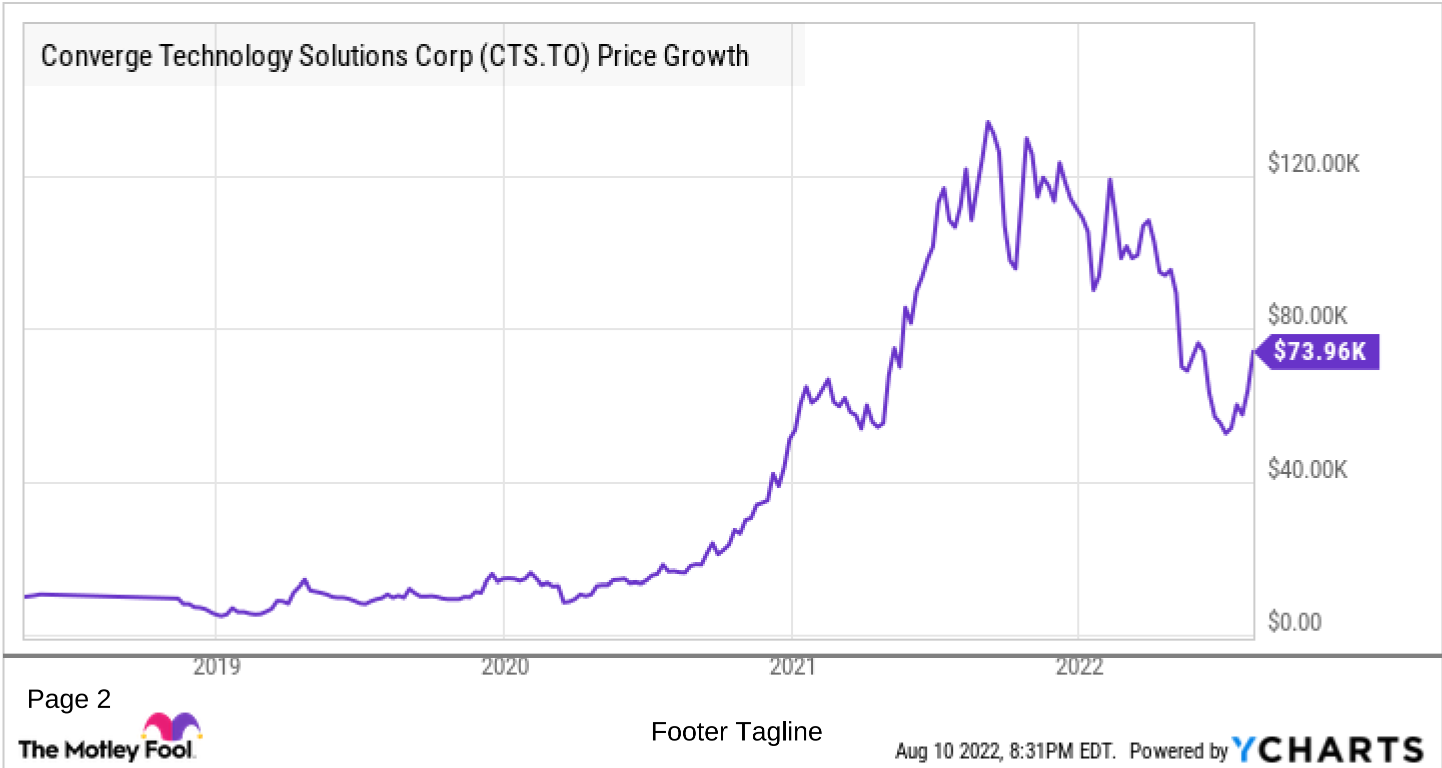
Year to date, the tech company has made eight acquisitions, picking up about $939.2 million of last-12-month gross revenue and $56.0 million of EBITDA. Acquisitions remain a key part of its growth plan. Thankfully, its balance sheet is still in good standing with little long-term debt. Long-term debt to total assets was about 9%.

The growth stock is still cheap

Converge CEO Shaun Maine stated, “Despite the macroeconomic challenges faced in the consumer market, business demand for digital transformation and hybrid IT solutions remains robust while the deep technical skills that Converge possesses surrounding analytics, cybersecurity, cloud and managed services remain scarce, especially in the mid-market.”

Indeed, “deep technical skills” are especially in demand in the mid-market space versus the large market, as bigger companies have the resources to hire in-house IT talent, while smaller companies may have other priorities.

Other than having a long growth runway, importantly, the tech stock is still [cheap](). According to *Yahoo Finance*, 12 analysts have an average 12-month price target of $11.10 per share, suggesting a substantial discount of 36%. Actually, the rally may indicate that the growth stock can be worth much more. Over the short term, we will probably see some analyst upgrades potentially to the $13 level.



CTS data by YCharts

That said, mid-cap stocks are typically more volatile. The above graph shows the growth trajectory of an initial $10,000 investment in Converge stock. Investors should note that short-term profit taking could take place in the stock as traders sell on good news. Long-term investors could get much wealthier with this stock, though, because, as illustrated in the article, the mid-cap stock has strong growth prospects.

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