



Stock Pick of the Week: Amdocs (DOX)

Amdocs (DOX) is not the kind of software company that finds itself in the headlines. Instead of explosive revenue growth and founders fresh out of the dorm room, Amdocs offers investors an extremely well run business with an enviable market position.

Amdocs specializes in software and services to manage customer care, billing, and order management for telecommunications companies. Amdocs derives much of its revenue from big wireless carriers such as AT&T (T) and Vodafone (VOD).

What Makes Amdocs a Special Software Company?

While Amdocs doesn't possess the rapid revenue growth of many software companies (ie. Netsuite (N), Salesforce.com (CRM)), its sales growth is nothing to sneeze at. Over the past decade, the company has grown revenue by 9% compounded annually, and by 5% compounded annually since 2010. Amdocs has managed to turn this top line growth into profit, and has grown its after-tax profit (NOPAT) by 12% over the past decade. In a market filled to the brim with high revenue growth technology companies, it's nice to find a company that can turn that revenue into profit.

Part of the reason for Amdocs' successes in the top and bottom line is management's excellent capital allocation skills. The company boasts a 12% return on invested capital (ROIC), and has maintained a stable NOPAT margin right around 12% every year since 2007. There are few signs that make us more confident in a business than a history of smart capital allocation and cost control.

This Year is Better Than the Last

2014 is falling right in line with Amdocs' historical trends. The company grew revenues 7% in 3Q14 over the same quarter last year, and revenue for the entire year is up 7% year to date. Operating income also increased 3% quarter over quarter in 3Q14, and for the full fiscal year up to this point as well.

Industry Climate Spells Success

Amdocs has long been recognized as the market leader in the overall billing market, and is continuing to grow its business. Amdocs controls between 18 and 24 percent of the overall billing market according to analyst firms Analysys Mason and Frost and Sullivan. The company's history of aggressively reinventing itself has allowed it to produce consistent returns in a hotly contested market. Most recently, Amdocs acquired the mobile network optimization solutions provider Actix Ltd. and self-organizing network provider Celcite. Amdocs is expanding into emerging markets where revenue increased 50% from 2011 to 2013, accounting for 12.3% of the company's revenue in 2013.

Amdocs' core business blends independent software vendor style products and integrated systems applications and services making for a more extensive and sticky relationship with clients.

Europe and the rest of the world also represent a large growth opportunity for Amdocs. Liberty Global, an international telecommunications company, and world's largest international cable company, recently announced that it would use Amdocs to support the expansion of its TV/internet/phone bundle offer in three European locations.

While consolidation is happening among telecom providers stateside, wireless providers are still clamoring for customers and expanding their networks around the world. As telecommunications demand increases, wireless systems will get larger, data stored will become greater, and Amdocs will be able to offer a number of products that help streamline business and maintain efficiency.

Room for Stock Price Growth

Given all this information, it is surprising to see how undervalued Amdocs is. At its current price of ~\$48/share, Amdocs has a price to economic value (PEBV) ratio of 1.0. This ratio implies the market expects Amdocs to never meaningfully grow NOPAT for the remaining life of the business. Amdocs has proven its ability to grow NOPAT consistently, and continues to do so in 2014; we feel these expectations are far too low.



If we assume Amdocs can grow NOPAT by 5% for the next 10 years, the stock is worth \$61/share – a 30% upside. This assumption is well below Amdocs' historical 10-year growth rate as well as its growth rate this year. With the continued expansion of wireless and telecom usage around the world, we feel confident in Amdocs' ability to continue growing NOPAT at or above its previous levels.

Kyle Guske II and Sam Andrews contributed to this article

Disclosure: David Trainer, Kyle Guske II and Sam Andrews receive no compensation to write about any specific stock, style, or theme.

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