Spotlight switches to small-cap technology stocks

BY AMANDA LANG
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Despite some recent share price dips, blue-chip technology stocks continue their relentless march.

As their trading multiples become harder to justify, market watchers say the spotlight is now turning to small-cap technology stocks, which often offer better value.

However, some junior technology firms may be too small to cash in on all the new attention. They may have good technology, or a good business model, but their market value puts them off the radar screen for many institutional investors and brokerage firms.

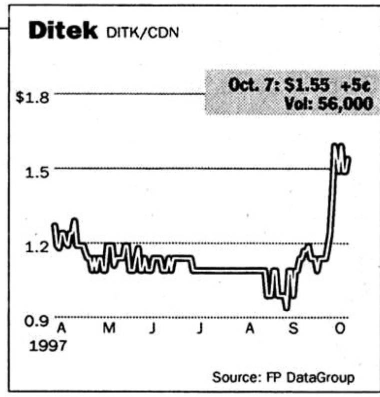
Smaller companies might even find it more difficult to raise cash in the current climate, company officials say. In a time of extraordinarily high cash inflows into mutual funds, and huge volumes of trading on equity exchanges, some small companies find their capital needs are just too small.

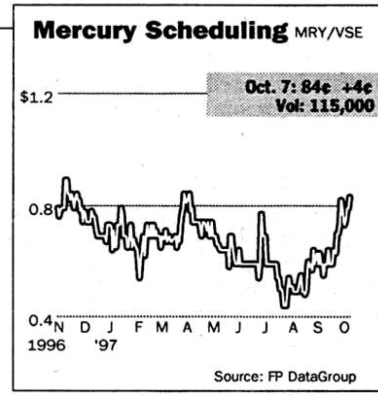
"These days, investment houses are looking to place tens of millions [of dollars], so if the financing you need is small, investors are not interested," says Ted Konyi, chief financial officer of Vancouver-based Mercury Scheduling Systems Inc.

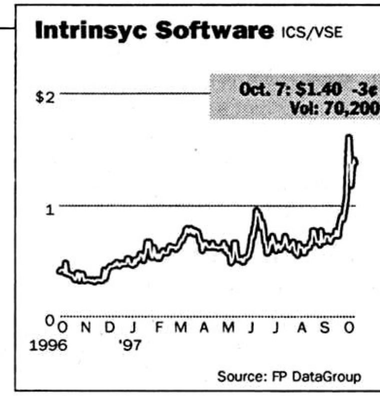
Micro-cap technology companies also carry a double virtue of being less sensitive than their big-cap rivals to stock market corrections — many do not have far to fall — while offering a bargain basement price.

Here are a few examples:

◆ **Ditek Software Corp:** Toronto-based Ditek was founded in 1985 by Oren Asher, who also formed Toronto-based MGI Software Corp.







Ditek makes software for computer-aided design, a market dominated by giant U.S. software maker of AutoCad, Autodesk Inc.

The company's strategy has been to work with third-party software developers. It licenses its core technology so they can add industry specific bells and whistles.

"People have called us crazy for trying to take on Autodesk," says Ditek chief executive Amnon Zohar. "But we are working with the people Autodesk was alienating," including developers who found the U.S. giant was invading their specialized markets. One such developer is Toronto-based Enghouse Systems Ltd., which incorporates Ditek's software in its mapping programs.

Ditek also sells its own CAD software, DynaCadd, which is about one-third of the price of a similar AutoCad product. The price differential has won it customers. Recently, publishers Addison Wesley Longman Inc. said it would replace AutoCad products with Ditek software in more than 1,000 bookstores across North America.

In the nine months ended May 31, Ditek reported net earnings of $473,000 (3¢ a share) on revenue of $1.7 million.

Ditek shares (DITK/CDN) have traded at between $1 and $1.20 since their initial public offering in March. The stock closed at $1.55 yesterday, up 5¢.

◆ **Intrinsyc Software Inc:** Shares of the Vancouver-based software company began to take off two weeks ago on rumors it was forming an alliance with Microsoft Corp.

However, William Yu, Intrinsyc's chief financial officer, scotched the rumors, saying Intrinsic's software has been recognized by Microsoft, but there is no formal partnership.

Yu says the share price increase is the result of almost a year of steady work in developing the company's software, which is the only product that transforms Microsoft's Windows CE software — used on small hand-held devices — into a Web server.

Intrinsyc stock (ICS/VSE) has traded at between 50¢ and 75¢ for the past 12 months, but shot up to $1.63 last week. The shares closed yesterday at $1.40, down 3¢.

◆ **Mercury Scheduling Systems Inc:** The company completed its initial public offering in August 1996, with shares priced at 80¢ each.

The firm has about 12 million shares outstanding, fully diluted, of which about 70% are held by principals of the company.

The shares (MRY/VSE) traded as low as 45¢ last July, before returning to their offering price. They closed up 4¢ at 84¢ yesterday.

Mercury chief executive Ted Konyi says it is only a matter of time before the shares take flight.

The company makes software that handles scheduling for airlines.

Although its revenue is small — $1.2 million in fiscal 1997 (ended April 31) — it competes on an equal footing with much larger companies that produce similar products.

Konyi says Mercury's software is superior to its rivals. The firm's high-end version of its software, called Magellan, is now in testing and sales should begin by spring.

In the near term, Mercury expects to announce distribution deals with at least two major airlines. That means airline software development groups will sell Mercury products to their feeder airline clients. Royalty revenue carries an extremely high margin, so profit on these arrangements is assured.

◆ **Enghouse Systems Ltd:** Months of strategic planning exercises at the software maker seems to be paying off.

The company's stock (ENGX/CDN) has climbed from $1.90 a year ago to a high of $10.13 last week. The shares closed yesterday at $8.37, up 12¢.

Enghouse makes CAD software used by utilities and cable companies to help them track their networks.

Its products CableCad and GeoNet have been bought by many telecommunications and cable companies in Canada and the U.S., and deregulation of those industries will help open up the market.

In the nine months ended July 31, Enghouse reported revenue of $31.6 million, up from $9.8 million a year earlier. Net income climbed to $1 million (13¢ a share), from a loss of $2.4 million (34¢) the year before.

"Not only is this a software company," says chief executive officer, Claudette MacKay-Lassonde, "but it is also a turnaround company.

"The growth we have experienced comes in part from that."

MacKay-Lassonde does not make projections about future revenue or profit, explaining that she did once "and got burned." However, she aims to propel Enghouse into the top-10 list of software companies in Canada within three years.