



TSS, Inc. (NASDAQ: TSSI)

CONVICTION NOTE · *The Selloff Misread the Print — Reaffirming Our Position*

FROM	DATE	RE	INTERNAL RATING
Mission Vertical Capital Investment Team	May 19, 2026	Q1 CY2026 results Reported May 7, 2026	HOLD — Conviction Maintained

POSITION SNAPSHOT

Stance	We continue to hold; conviction on thesis remains intact following post-print weakness
Position role	Core AI-infrastructure compounder — small-cap sleeve
Recent price	~\$11–\$12 (vs. ~\$16 pre-print; 52-wk range \$6.87–\$31.94)
Reference consensus	Needham CY26E: Revenue \$198.0M / Adj. EBITDA \$21.9M
What changed	Nothing in the thesis — the market repriced optics, not fundamentals

The Bottom Line

TSSI fell sharply after a quarter that, on the metrics that matter, came in on plan. Adjusted EBITDA of \$5.3M beat the Street's \$4.0M estimate, full-year guidance was reaffirmed toward the high end, and the systems-integration engine grew 88%. The 44% headline revenue decline was procurement — the lowest-margin, lumpiest line in the business — lapping a record comp. We read the selloff as a sentiment dislocation, not a thesis break.

1. THE QUARTER THE HEADLINE MISSED

The headline was a 44% year-over-year revenue decline, to \$55.3M from \$99.0M. That number, in isolation, is what moved the stock. But it conflates two very different businesses. Procurement — a low-margin, pass-through agency line — fell 56% to \$40.0M against a genuinely extraordinary \$90.2M comp a year ago. Management has been consistent that the prior-year figure was an anomaly and that procurement should run at a \$30–\$35M quarterly pace; on that framework, Q1 was actually ahead of the ~\$32M implied baseline. Punishing the stock for procurement normalizing is like marking down a homebuilder because it resold less lumber.

Underneath that, the part of TSS that actually creates value did exactly what the thesis calls for. Systems integration grew 88% to \$14.1M and now represents 25% of revenue, up from 8% a year ago. Segment gross margin expanded more than fifteen points, to 37.5%. The reported ~1% sequential dip in that line was an optical artifact — the prior quarter carried roughly \$1.8M of one-time catch-up revenue; normalized, systems integration grew approximately 14% sequentially. Profitability landed on plan: adjusted EBITDA of \$5.3M beat the Street's \$4.0M estimate, with EBITDA margin expanding to 9.5%. The company reaffirmed full-year adjusted EBITDA guidance of \$20–\$22M and indicated it expects to finish at the high end.

**Q1 CY2026 against the prior year and the post-print consensus:**

Metric	Q1 CY26	Q1 CY25	Street Est.
Total revenue	\$55.3M	\$99.0M	\$43.2M
Procurement revenue	\$40.0M	\$90.2M	~\$32M
Systems integration revenue	\$14.1M	\$7.5M	\$9.5M
Gross margin	15.9%	9.3%	15.9%
SI segment gross margin	37.5%	22.1%	—
Operating income	\$2.3M	\$2.6M	\$1.2M
Adjusted EBITDA	\$5.3M	\$5.2M	\$4.0M
Adj. EBITDA margin	9.5%	5.3%	9.3%
GAAP EPS	\$0.08	\$0.12	\$0.03

Source: Company reports; reference consensus per Needham post-print model (May 8, 2026). Q1 CY25 procurement comp was a record the company has characterized as an anomaly.

A Street-beating EBITDA print, a reaffirmed and high-end-biased full-year outlook, and a margin structure moving in the right direction — met with a 20%-plus selloff. That is the dislocation the thesis is built around.

2. THE RACK BUSINESS IS THE ENGINE — AND IT IS ACCELERATING

Strip out procurement noise and the trajectory is unambiguous. Systems integration is scaling, and the volume signal from the earnings call was the most important data point of the quarter: management stated that within the month, TSS will have completed more rack integrations in 2026 than it delivered in all of 2025. That is a remarkable throughput statement only four months into the year. Georgetown still has meaningful headroom — management believes it can do multiples of current rack volume in the existing footprint, with validation-test time as the real bottleneck the team is actively working to compress.

Two structural features of the customer agreement underpin why this trajectory is viewed as durable rather than a one-quarter event:

- **Downside protection, with the real upside still ahead.** The long-term agreement carries guaranteed minimum payments that cushion volume air-pockets. More importantly, management was explicit that until weekly volumes clear those minimums, the revenue uplift is muted — and then it gets "much more dramatic." Needham frames this as roughly a 4x revenue multiplier once the minimum weekly shipment threshold is cleared. TSS has cleared it only occasionally so far. The convexity in this model has not yet shown up in the numbers.



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- **Each capacity expansion resets pricing upward.** The December 2025 amendment re-priced the agreement to recapture TSS's prior CapEx and added power. The next reset is already in motion: the customer has requested roughly \$17M of additional CapEx to support next-generation racks — Needham specifically attributes this to Vera Rubin-class GPU infrastructure — with assets expected in use by Q3 CY26 and pricing recapture beginning shortly after. This is a recurring margin escalator, not a one-off.

A third leg was added May 1: the previously idle Round Rock facility has been dedicated to warehousing AI-rack material for the anchor customer, and that contribution is already inside guidance.

3. THE DELL HIRES — THE MOST UNDERAPPRECIATED DEVELOPMENT IN THE STORY

On April 28, TSS named two new C-suite executives. Matt Wallace joins as Chief Strategy Officer after a 13-year tenure at Dell Technologies, most recently as Vice President of Corporate Strategy & Market Intelligence. David Hull joins as Chief Technology Officer with nearly 29 years at Dell, most recently as Senior Director, CTO Technology Strategy.

Hull's background is not generic. At Dell he served as Systems Engineering Director for Cloud, AI and Emerging Technologies, directing the architecture and delivery of next-generation server platforms — including industry-first rack-scale AI servers for hyperscale customers. TSS has hired the person who helped design the rack-scale AI servers TSS is now paid to integrate. Three reasons this matters to the position:

- **It institutionalizes the anchor relationship.** TSS does not name its anchor customer, but the dependency is near-total at 99% of revenue. Bringing in two senior Dell veterans — one from corporate strategy, one from CTO-level engineering — is functionally a move to deepen and de-risk the single most important commercial relationship the company has.
- **It makes the beyond-OEM expansion credible.** Management was explicit that there is a large part of the market today's OEMs do not serve — the whitebox rack-integration opportunity — and that TSS intends to pursue it. A CSO from Dell corporate strategy knows precisely where that white space sits; a CTO who built hyperscale rack-scale platforms knows how to build the capability to serve it. These hires convert customer-concentration risk from a static liability into an addressable problem.
- **It de-risks the technical roadmap.** The \$17M next-gen CapEx cycle, the shift toward optical networking inside the rack, the validation-time bottleneck — these are squarely Hull's domain. As the technical burden migrates from chip vendors down to integrators, TSS has the engineering leadership to absorb it.

4. DELL'S PIPELINE IS THE DEMAND BACKDROP — AND IT IS EXPLODING

If the anchor relationship is Dell-linked, then Dell's order book is TSS's leading indicator. For its fiscal year ended early 2026, Dell closed more than \$64 billion in AI-optimized server orders, shipped more than \$25 billion, and entered the new fiscal year with a record \$43 billion backlog. AI backlog moved from \$18.4B at the end of fiscal Q3 to \$43.0B one quarter later, with \$34.1B of AI orders booked in that single quarter alone.

The forward guide is what matters most: Dell has guided full-year AI-optimized server revenue to roughly \$50 billion, up approximately 103% year over year. The pipeline is broadening — Dell now serves more than 4,000 AI customers across enterprises, neoclouds, sovereigns, and government, with a five-quarter pipeline described as



multiples of even that record backlog. Dell's stated competitive differentiator is rack-scale deployment speed — racks operational within 24–36 hours. When a customer's edge is integration velocity, its integration partners are direct beneficiaries of every order booked.

A \$43B backlog and a ~\$50B forward AI-server plan represent a multi-year wave of rack volume that has to be physically integrated somewhere. TSS's Georgetown facility, with room to grow throughput several-fold, is positioned to capture a rising share. The honest caveat: AI-server demand is non-linear. The backlog supports the direction of travel; it does not smooth the quarterly path.

5. VALUATION: TSS AGAINST ITS PUBLIC PEERS

To pressure-test whether the post-print price makes sense, we set TSS alongside the public companies that sit nearest to it on the AI-infrastructure value chain — Super Micro, Penguin Solutions (the closest pure analog), HPE, and Dell.

Company	Description	Market Cap	EBITDA Margin	EV/EBITDA
TSS (TSSI)	AI-rack integration + facilities + procurement	~\$0.3B	~10%	~12–13x
Super Micro (SMCI)	AI-optimized server OEM / manufacturer	~\$18B	~6%	~17x
Penguin Solutions (PENG)	AI data-center systems integration & infra	~\$2.4B	~10%	~12x CY26E
HPE	Diversified server, storage & networking OEM	~\$40B	~13%	~12x
Dell (DELL)	Server & PC OEM; TSS's anchor customer	~\$115–170B	~7–8%	~13–15x

NTM / CY26E EBITDA for TSS and PENG; trailing figures for SMCI, HPE, and Dell. Multiples are approximate and shown for orientation, not precision.

Server OEMs — Super Micro, HPE, Dell — manufacture and sell the box, carry inventory and component-cost risk, and earn high-single-digit to low-teens EBITDA margins. Super Micro's consolidated ~6% margin is essentially the same as TSS's procurement-segment margin — the lowest-quality line TSS runs. TSS's systems-integration segment earns 37.5% gross margin because it sells engineering, labor, and validated throughput rather than hardware; most integration components are consigned by the customer and never touch TSS's balance sheet. As TSS's mix shifts toward integration, it migrates away from box economics toward a higher-margin, lower-capital services model.

Penguin Solutions is the most instructive comparison — an AI data-center infrastructure and integration business with EBITDA margins nearly identical to TSS's. PENG's EBITDA is forecast to grow roughly 8% this year to ~\$200M and a further ~16% next year to ~\$232M, placing the stock at approximately 12x this year's EBITDA and ~11x forward. TSS's systems-integration segment is growing far faster — revenue up 88% year over year. A faster-growing, higher-margin integration business should command a higher multiple than PENG, not a lower



one. Yet on CY26 EBITDA, TSS trades at roughly 12–13x — in line with PENG's current-year multiple — and on a high-\$20Ms forward number it falls to ~9–10x, a clear discount to PENG's ~11x forward. The growth differential argues the relationship should run the other way.

How we frame the range:

Scenario	EBITDA	Multiple	Implied EV	Equity Value	/ Share
CY26 in line	\$22M	14x	\$308M	\$357M	~\$12.50
CY26 modest beat	\$24M	16x	\$384M	\$433M	~\$15
Forward, high-\$20s	\$28M	18x	\$504M	\$553M	~\$19–20
Forward + peer-group re-rate	\$28M	20x	\$560M	\$609M	~\$21–22

Equity value adds ~\$49M net cash; per-share on ~28–29M diluted shares. Illustrative scenario analysis, not a price target.

If TSS beats CY26 EBITDA even modestly and then grows into the high-\$20Ms, a 16–20x EV/EBITDA range — inside the band where OEM peers trade today, and a deserved premium to a slower-growing Penguin Solutions at ~11x forward — is defensible, framing a stock worth roughly \$18–\$22 against ~\$11–\$12 today. That is broadly consistent with Needham's Buy rating and \$16 target — a target set on CY26 numbers that gives little credit to the forward EBITDA ramp.

6. KEY RISKS TO THE THESIS

The position is held with discipline, not uncritically. Key signals to monitor:

- **Customer concentration.** One OEM is 99% of revenue and 88% of receivables. The Dell hires mitigate this; they do not erase it. A loss or material breach of the anchor agreement would leave TSS holding facility lease and debt service regardless of revenue. This is the dominant risk.
- **Unremediated material weakness.** The internal-controls material weakness identified in the 2024 audit remains open. Management states the financials are fairly presented and remediation is underway, but it is a real overhang for institutional ownership.
- **Procurement-driven optics.** The Q1 headline dynamic will recur whenever a large prior-period procurement quarter is lapped. The stock clearly trades on reported revenue, so further sentiment-driven air-pockets should be expected.
- **Power and execution risk.** Georgetown's contracted power is finite; each GPU generation draws more. Scaling depends on securing incremental power and cooling and on compressing validation-test time. A stall there would cap the volume convexity underwritten by the thesis.



OUR POSITION

The quarter did not break the thesis — it created a gap between price and fundamentals. The earnings engine grew 88% with fifteen points of margin expansion, EBITDA beat the Street and the full-year guide was reaffirmed toward the high end, two senior Dell executives joined to deepen the anchor relationship and open the whitebox market, and the demand backdrop — Dell's \$43B AI backlog and ~\$50B forward plan — is as strong as it has been.

Set against its public peers — Super Micro at ~17x, Dell and HPE in the low-to-mid teens, and its closest analog Penguin Solutions at ~12x this year and ~11x next — TSS at ~12–13x current and ~9–10x a plausible forward number trades at the low end of the group despite the fastest growth and arguably the best earnings quality in it.

The concentration risk and the open material weakness are real, and they inform position sizing discipline. On the analysis presented here, the risk/reward at current prices is favorable. We will update as the CapEx cycle completes in Q3 and as volumes test the contract minimums that gate the real upside.

DISCLOSURE

This note is prepared by Mission Vertical Capital for informational purposes only. It is not investment, legal, or tax advice and is not an offer or solicitation to buy or sell any security. Reference consensus figures are drawn from Needham & Company (May 8, 2026); Dell and Super Micro figures are drawn from company filings and public reporting. Forward estimates are illustrative scenario analysis, not price targets, and actual results may differ materially. Past performance is not indicative of future results.