



Is Constellation Software Inc. a Buy After its Strong Q3 Report?

Description

Constellation Software Inc. ([TSX:CSU](#)), one of leading providers of software and related services to a select group of public and private sector markets, announced third-quarter earnings results after the market closed on October 28, and its stock has responded by making a slight move to the upside. Let's break down the quarterly results to determine if the stock could continue higher from here and if we should consider initiating long-term positions today.

Acquisitions lead to very strong top- and bottom-line growth

Here's a summary of Constellation's third-quarter earnings results compared with what analysts had expected and its results in the same period a year ago. All figures are in U.S. dollars.

| Metric | Q3 2015 Actual | Q3 2015 Expected | Q3 2014 Actual |
|-----------------------------|------------------|------------------|------------------|
| Adjusted Earnings Per Share | \$4.67 | \$4.22 | \$3.27 |
| Revenue | \$460.36 million | \$467.40 million | \$418.81 million |

Source: *Financial Times*

Constellation's adjusted earnings per share increased 42.8% and its revenue increased 9.9% compared with the third quarter of fiscal 2014. These very strong results can be attributed entirely to the company's acquisition activity over the last year, which contributed \$63 million in revenue in the third quarter, including \$40 million in its public sector segment, and \$23 million in its private sector segment, and this more than offset its negative 5% organic growth.

It is also worth noting that the company was heavily impacted by changes in foreign exchange rates, which reduced its organic growth by 6%.

Here's a quick breakdown of 10 other notable statistics from the report compared with the year-ago period:

1. Adjusted net income increased 42.7% to \$98.9 million

2. Revenue increased 7.3% to \$316.4 million in its public sector segment
3. Revenue increased 16.1% to \$144 million in its private sector segment
4. Maintenance and other recurring revenues increased 15.7% to \$298.5 million
5. Professional services revenues decreased 7.6% to \$91.99 million
6. Hardware and other revenues increased 11% to \$36.57 million
7. Licensing revenues increased 17.4% to \$33.3 million
8. Adjusted earnings before interest, taxes, and amortization (EBITA) increased 20.1% to \$120.3 million
9. Adjusted EBITA margin improved 220 basis points to 26.1%
10. Net cash flows from operating activities increasing 4% to \$105.1 million

Constellation also announced that it will be maintaining its quarterly dividend of \$1.00 per share, and the next payment will come on January 5 to shareholders of record at the close of business on December 17.

Should you buy shares of Constellation Software today?

The third quarter was a great success for Constellation Software, so I think its stock has responded correctly by moving higher.

I also think it represents a very attractive long-term investment opportunity today, because its stock still trades at inexpensive valuations, including just 34.8 times fiscal 2015's estimated earnings per share of \$16.04 and only 28.9 times fiscal 2016's estimated earnings per share of \$19.27, both of which are inexpensive compared with its trailing 12-month price-to-earnings multiple of 73.4 and its five-year average multiple of 40.7.

With its average price-to-earnings multiples and the 19.4% long-term growth rate in mind, I think Constellation's stock could consistently command a fair multiple of at least 40, which would place its shares upwards of \$770 by the conclusion of fiscal 2016, representing upside of more than 38% from current levels.

With all of the information provided above in mind, I think Foolish investors should strongly consider beginning to scale in to long-term positions in Constellation Software today.

CATEGORY

1. Investing
2. Tech Stocks

TICKERS GLOBAL

1. TSX:CSU (Constellation Software Inc.)

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Date

2025/09/30

Date Created

2015/10/29

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