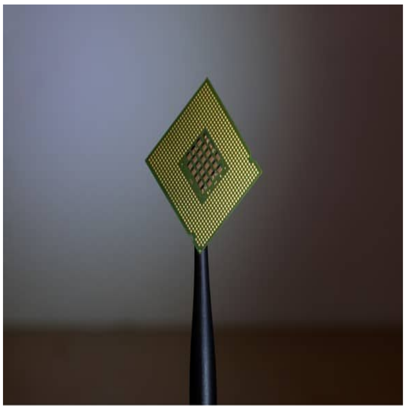

Is it Time to Get Back Into Canadian Tech Stocks?

Description

Canadian technology stocks were riding high just a few months ago. The **S&P/TSX Capped Information Technology Index** hit an all-time high of $87 in July. Now the index is down to $71.6.

The index is on the verge of a technical bear market, which is defined as a 20% or more drop from all-time highs. This could mean it's a great time to take a closer look at Canada's finest technology companies to seek out bargains.

Shopify (TSX:SHOP)(NYSE:SHOP) is probably the most interesting tech stock in the country at the moment. The company recently announced stellar growth in its third-quarter results. Revenue was up 58% from the same period last year and the company's management guided for full-year revenue slightly over US$1 billion.

The stock was up over 11% the very next day. It's hard to deny the appeal of a business with a solid network of users and monthly recurring revenue. However, long-term investors are still disappointed by the lack of cash flow, profits, and slowing growth.

Technology stocks are always growth plays, which is why Shopify still trades at a price-to-sales (PS) ratio of nearly 15.8 times. However, **Amazon** trades at a PS ratio of less than four times and delivers consistent positive cash flow. That means Shopify is comparatively overvalued.

Constellation Software (TSX:CSU) is another high-flying tech stock that has been recently beaten down. At the current price of $868, it's down 23.5% from its all-time high earlier this year.

Since it went public in 2006, this tech company has gobbled up nearly 300 small- and medium-sized software firms and delivered a jaw-dropping 3,000% return to shareholders.

Constellation is a very atypical technology company. Instead of investing in research, product development, and marketing, the CEO Mark Leonard is trying to create the **Berkshire Hathaway** of the software world. This means this recent downturn in valuations should be great for the company's acquisition-driven business model.

If the company is trying to create a tech conglomerate, I guess traditional value investing like price-to-free cash flow (P/FCF) and price-to-book (PB) ratios are best suited. Constellation currently trades at a P/FCF of 24.8 times and a PB of 20.7 times. For a technology company, I think those ratios are brilliant.

Finally, **Kinaxis** (TSX:KXS) is trading 14% off its all-time high. The supply chain management and sales and operation planning software company has a list of high-quality clients signed up for recurring services. With thousands of potential clients and a market worth US$4.4 billion, it has plenty of room for growth.

However, at a PE ratio of 86.25, the company will need to deliver 86% growth to hit a justifiable PEG ratio. I believe that is far-fetched and the stock is still overvalued.

The bottom line

Technology companies need to justify their high valuations with incredible growth. Of the three stocks I've picked here, only Constellation strikes me as fairly valued. However, if the downturn in stock prices continues, many of these stocks could get more attractive.

CATEGORY

1. Investing
2. Tech Stocks

TICKERS GLOBAL

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2. TSX:CSU (Constellation Software Inc.)
3. TSX:KXS (Kinaxis Inc.)
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