



This Canadian Tech ETF Has Beaten the S&P 500 by a Huge Margin

Description

Technology stocks have always been one for the masses. Due to their high-growth metrics, tech companies have been an investor favourite. Further, the everyday use of these products brings a sense of familiarity for retail investors.

However, tech stocks tend to be very volatile. Due to the ever-changing landscape in tech and continuous disruption, what might seem like a major win today could very well be obsolete tomorrow. So, how do investors take advantage of tech stocks?

Well, retail investors can look to invest in technology-based exchange-traded funds (ETFs). As we know, ETFs provide diversification, as they hold a basket of stocks. One such ETF is **iShares S&P/TSX Capped Information Technology Index ETF** ([TSX:XIT](#)).

According to a BlackRock report, “The iShares S&P/TSX Capped Information Technology Index ETF seeks to provide long-term capital growth by replicating, to the extent possible, the performance of the S&P/TSX Capped Information Technology Index, net of expenses. The index is comprised of constituents of the S&P/TSX Composite Index in GICS Sector 45 — Information Technology.”

The XIT has easily outperformed the **S&P 500** since March 2006. This ETF has risen from \$6.51 in March 2006 to its current price of \$26.44, indicating stellar growth of 11% annually. Comparatively, the S&P 500 has risen under 7% annually in the same period. So, what drove this ETF higher?

The top two holdings of XIT include **CGI** ([TSX:GIB.A](#))([NYSE:GIB](#)) and **Constellation Software** ([TSX:CSU](#)); they account for almost 50% of this ETF. These stocks have been key drivers for XIT.

CGI

Shares of CGI have been winners all the way. The stock went public in September 1996. It has seen two major recessions in the last two decades and created significant investor wealth. CGI stock rose from \$0.38 in September 1996 to \$30.88 in December 1999.

It then fell to \$7.75 in March 2006. The stock has since gained an impressive 1,250% since then to trade currently at \$106. CGI stock is valued at \$28.6 billion. It provides services primarily in IT consulting and systems integration.

While CGI stock has gained exponentially in the past, does it have enough upside potential to excite investors? Analysts expect CGI to increase sales by 5.3% to \$12.75 billion in fiscal 2020 (ending in September) and by 3.6% to \$13.21 billion in 2021.

CGI stock is trading at a forward price-to-earnings multiple of 19 times. Comparatively, analysts expect earnings to rise by 10.2% in 2020, 7.9% in 2021, and at an annual rate of 10.6% over the next five years.

CGI stock seems overvalued at the current price looking at these metrics and might move lower in a sell-off. Analysts have a 12-month average target price of \$110.5 for CGI, which is 3.8% above the current price.

Constellation Software

CSU is another Canada-based tech heavyweight. The stock has gained a staggering 5,200% since its IPO back in October 2007. However, these returns have meant that CSU stock is also trading at an expensive multiple.

Analysts expect CSU to increase sales by 13.8% to \$3.48 billion in 2019 and by 16.4% to \$4.06 billion in 2020. CSU stock is trading at a forward price-to-earnings multiple of 35.7 times. Comparatively, analysts expect earnings to rise by 3.2% in 2019, 24.4% in 2020, and at an annual rate of 15% over the next five years.

Analysts have a 12-month average target price of \$1,112.58, which is 14% below the current price. I had identified CSU as an [overvalued stock last month](#), and it has fallen close to 5% since then.

While the two Canadian tech giants remain solid long-term picks, their current valuation makes little sense.

Do you bet on XIT going forward?

While XIT has been one of the most successful tech ETFs in terms of absolute returns over the last decade, it is primarily banking on two stocks, both of which are vulnerable in a downturn.

So, how do investors play this ETF? Well, they need to buy XIT at major dips and invest over the long term.

CATEGORY

1. Investing
2. Tech Stocks

TICKERS GLOBAL

1. NYSE:GIB (CGI Group Inc.)
2. TSX:CSU (Constellation Software Inc.)
3. TSX:GIB.A (CGI)
4. TSX:XIT (iShares S&P/TSX Capped Information Technology Index ETF)

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