Buyer Beware: Are These 2 Tech Stocks Ridiculously Expensive Today?

Description

Canadian growth stocks, especially in the technology sector, have been having a great run over the past few years. Many of these stocks have doubled over the past several years, leaving long-term investors with some pretty incredible gains. But is there still room for the stocks to run, or should investors take the money and run right now?

One of the stocks that fit this category at the moment is the supply chain software solutions provider, **Kinaxis Inc.** (TSX:KXS). A year ago I wrote that this company was excellent with a high growth rate, but was enormously overpriced. At the time I recommended waiting for a pullback to begin establishing a position.

Well, the pullback came and the stock dipped significantly from nearly $100 a share to around $60. If you had used that point to enter the name, you'd now be sitting on a gain of around 80% as the stock ripped sharply back upwards to today's market price of over $100.

Apart from being a strong stock performer, Kinaxis has also been posting some pretty strong financial results. In the third quarter of 2019, the company reported a 29% increase in its year-over-year total revenue.

Gross profit grew by 36%, a very healthy gain for a growing company. Kinaxis also has no debt and a ton of cash, so it should be in pretty good shape if the economy turns sour.

Another technology company that has made some healthy gains is **Constellation Software Inc.** (TSX:CSU). I've been watching this stock for years as it has continued to rocket higher with a 56% gain over the last year alone.

This grow-by-acquisition story has been a very good performer over the past several years, although it remains to be seen whether its fortunes will stay positive.

Constellation Software acquires companies, manages them, and builds them up into a market-leading business. These subsidiaries cover a wide array of industries, from hospitality to oil and gas.

With all these businesses under its belt Constellation Software has also managed to increase many of its financial metrics by the double digits. Its revenue grew by 15% year-over-year, although the negative organic growth of -2% was a little troubling to see. Net income increased by 24% over the same time period and free cash flow available to shareholders increased by 20%.

Would I buy these companies today?

As someone who generally focuses on value, I always find it difficult to invest in stocks that command premium valuations. These companies certainly aren't cheap. Kinaxis trades at a P/E multiple of around 114 times trailing earnings, and Constellation, while somewhat cheaper, also trades at a high multiple of about 52 times earnings.

For me, valuations like this are reserved for very fast-growing companies that operate commanding positions in their field like **Google Inc.** (NASDAQ:GOOGL). While both Kinaxis and Constellation appear to be growing at a decent rate, I'm not as willing to pay up for these businesses at the moment.

I do like one aspect about both of these companies, though, and that is the quality of their balance sheets. Neither company has much in the way of net debt, and both have a healthy amount of cash.

If you're a growth investor, you might be interested in holding at these levels. But if, like me, you're more focused on value, I'd probably stay away from these expensive stocks for the time being. If there is another market pullback, you will likely get another chance to pick these up at a lower level.

CATEGORY

1. Investing
2. Tech Stocks

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

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