The Most Expensive Stock in Canada Is a Top Pick

Description

At times, investors put too much emphasis on a company's share price. I can't tell you how often I see investors asking for top picks under a certain dollar threshold such as $10.00 per share.

The logic appears sound: the lower the price, the more shares one can scoop up. Given that it has a low share price, the quicker it can double.

Investors are attracted to penny stocks for just such reasons. Unfortunately, these concepts are misplaced. In fact, an investor should never judge a company by its share price alone.

A lower-priced stock does not equate value and vice-versa — a higher priced stock does not equate to being expensive.

There are countless examples of this. In Canada, the best example is that of **Constellation Software** (TSX:CSU). At $1,350 per share, this software giant has the highest share price on the **TSX Index**.

Notice I didn't say expensive? Admittedly, the title is somewhat misleading, but it was purposefully so — a majority of retail investors would consider Constellation expensive.

The reality is that Constellation has been one of the highest priced stocks for a while now and yet, it continues to double. Over the past five years, the company's share price has soared by 295% and has achieved a 32.5% compound annual growth rate, placing it among the best perming stocks on the **TSX Index** despite starting the period at a price north of $300 per share.

Constellation was also the third-best performing stock of the last decade, gaining 3,355%!

In 2019, the company opened the year trading at ~$850 per share, and the share price has since gained another $500 (~58%). Simply put, Constellation is a best-in-class software company and a single share in the company can yield outsized returns.

Can Constellation's stock reach $2,000 per share? Yes, without question. This would imply 48% upside from today's price. Given its history of growing at a CAGR of 32%, it's entirely plausible that it could reach $2,000 per share within the next couple of years.

Let’s assume however, that the company grows inline with analysts earnings estimates, currently pegged at 15% annually over the next five years. At this rate, the company would achieve the mark in just under three years.

Current valuation

Let’s circle back to valuation: is the company expensive? Trading at 28 times forward earnings, the company certainly isn’t cheap. Is it expensive? Not when compared against the software industry average (forward P/E of 54) and Constellation’s own ability to exceed expectations.

It also has one of the highest net margins in the industry with a best-in-class management team that is often misunderstood. The company doesn’t hold quarterly conference calls, preferring to communicate via their AGM and a Q&A feature on its website. This makes it hard for analysts and investors who rely on instant access to information.

The shift away from quarterly conference calls should be lauded. At times, investors put too much emphasis on management’s on-the-spot responses to questions on these calls.

This forces investors to focus more on the long-term prospects of the company. An investment in Constellation requires a significant level of trust in management — trust that continues to be well placed, as Constellation has consistently proven to be one of the best industry consolidators.

It remains a top pick despite a high share price.

CATEGORY

1. Investing
2. Tech Stocks

TICKERS GLOBAL

1. TSX:CSU (Constellation Software Inc.)

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