This TSX Stock Is Resilient to the Pandemic

Description

Shopify became the ultimate virus stock, as the demand for its e-commerce solutions sky-rocketed amid the COVID-19 pandemic. It also became the first tech stock to cross the $100 billion market capitalization. Another stock that grew alongside Shopify was **Descartes Systems** (TSX:DSG)(NASDAQ:DSGX), Canada's largest cloud-based logistics and supply chain solutions provider.

Descartes provides cloud and on-premise logistics and supply chain management software. It caters to companies like airlines, logistics service providers, manufacturing, and e-commerce sites, for whom the transfer of goods, people, and information from one point to another is a significant part of their operations. It also offers end-to-end supply chain operations from sourcing to procurement to paying custom duties to inventory management to distribution.

Descartes will benefit from the growing complexities in supply chain management

The globalization of trade has added several participants to the supply chain. The rise of e-commerce led to the emergence of faster, cheaper, and flexible delivery options, creating planning and execution challenges in supply chain management. These are business events that companies can control. There are also macro events on which companies have no control.

For instance, the U.S.-China trade war has added several layers of regulatory complexity for companies having trade deals with China. Many customers are using Descartes's tariff and duty content and Denied Party Screening solutions to optimize their trade.

The biggest macro event is COVID-19 pandemic. It has changed consumer demand, restricted travel, and introduced new safety measures in the distribution of goods.

In its fiscal 2021 first-quarter earnings, Descartes noted that the pandemic-driven lockdown significantly hit passenger airlines, automotive, and retail stores. However, sectors like e-commerce, medical equipment, and grocery saw an uptick. As the economy reopens, logistics will be the biggest challenge, according to a PwC China report.

Descartes is well placed to help companies address the logistics challenges in the short term. Moreover, it will benefit from the growing complexities of business and macro events in the long term.

Descartes's diversified operations make it resilient to the pandemic

While Descartes is not entirely immune to the pandemic, its business is resilient to an economic downturn because of the diversified nature. The company serves a vast majority of customers, big and small, operating in different industries ranging from freight forwarders to manufacturers to retailers. Some of its customers include **FedEx** and **Home Depot**. It also has exposure to different modes of transportation, including air, water, road, and rail.

Beyond customers, Descartes has also diversified its service offerings, allowing customers to select some or all of its services. Some of its offerings include e-commerce shipping and fulfillment, transportation management, and customs and regulatory compliance. It has also diversified its pricing model to include perpetual licences, subscriptions, and transactional services. This diversification has enabled the firm to increase its revenue at an average annual rate of 12% between fiscal 2016 and 2020.

Descartes can withstand the pandemic with its strong fundamentals

Like all cloud-based services, Descartes's profits margins improve with economies of scale. Its adjusted EBITDA rose 10-15% every year for the last 10 years on the back of strong revenue growth. Between fiscal 2018 and 2020, it increased its adjusted EBITDA at a CAGR of 23%. Its EBITDA was driven by organic growth and through acquisitions.

As Descartes feels the pandemic's impact, it expects revenue to fall 4.4% YoY (year over year) in the second quarter of fiscal 2021. It is restructuring its cost structure as per the current demand, but it will realize the savings after six months. Hence, its adjusted EBITDA growth rate will take a hit in the short term.

When the lockdown eases and demand recovers, the firm could see a sudden surge in logistics and supply chain activities. The renewed demand could boost its long-term earnings, bringing the average adjusted EBITDA growth rate to 10-15%.

Descartes stock: Buy and hold for at least five years

Descartes stock rose 15% year to date, outperforming the **TSX Composite Index**, which fell 11%. If you had invested $10,000 in this tech stock in early 2015, your investment would have grown to $35,500, generating an average annual return of 29%.

Descartes's diversified business, strong fundamentals, and long-term growth opportunities show that it can duplicate the above returns in the coming five years. Moreover, its resiliency to an economic downturn will minimize your risk.

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TICKERS GLOBAL

1. NASDAQ:DSGX (Descartes Systems Group)
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