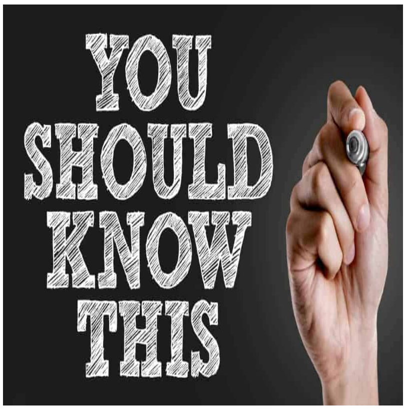


TSX Stocks: Analyzing Growth Stocks and PEG Ratios

**Description**

Growth stocks generally beat broader markets and thus trade at a higher valuation multiple. Take, for example, tech companies. They generate revenues, earnings, and cash flows at a superior rate and have higher profit margins than the average.

However, it is not prudent to get carried away just by the rosy outlook of the company and pay exorbitantly high.



## Are you paying too much for growth?

The tech giant **Shopify** (TSX:SHOP)(NYSE:SHOP) is a classic case of growth stocks. Its revenues have doubled at around 60% compounded annually in the last five years, and the stock has almost doubled every year in the same period.

What valuation multiple is reasonable, and what is considered as expensive then? Many growing companies do not generate profits, so valuing them based on price-to-earnings ratio becomes useless. The price-to-sales ratio also tells you half of the picture and overlooks growth prospects.

PEG ratio or price-to-earnings to expected growth ratio comes in handy in such cases. The ratio considers the current price to its earnings against its expected growth for the next few years. Thus, the PEG ratio should give a fairly clearer picture of which growth stocks to buy and which ones to avoid.

PEG ratio lower than 1.0 indicates the stock is undervalued, and above 1.0 suggests a red flag. It does not mean stocks with higher PEG ratios should be avoided altogether. But it might mean that you are paying higher for growth than reasonable.

## Top TSX stocks and PEG ratios

Well, enough of the theory. Let's look at some of the top growth stocks on the **TSX**. Consider Shopify. It is currently trading at $1,500 and boasts a price-to-earnings multiple of close to 600x. Even if Shopify continues to grow at the same pace for the next few years, that still won't justify its current valuation. Shopify stock looks astronomically overvalued at the moment.

It looks like investors are pretty convinced that Shopify could be the next **Amazon**. But interestingly, Shopify stock has carried the premium valuation for the last several years.

Another tech titan **Constellation Software** looks more reasonably valued compared to Shopify. Its PEG ratio comes around 3x and looks overvalued. However, it has also created massive wealth for shareholders in the last couple of decades.

Now consider a Canadian miner **B2Gold** (TSX:BTO)(NYSE:BTG). It operates three gold mines and produces around 1 million ounces of gold annually. Like many of its peers, B2Gold managed to double its earnings in 2020.

But that's not a one-off event. B2Gold has been growing its earnings at a far superior rate than the industry average. From $39 million in 2016, its net income has grown to $637 million in the last 12 months. That's a compound annual growth rate of an astounding 75%.

B2Gold stock is currently trading at $7.1, which implies a price-to-earnings multiple of 11.5x. Even if we assume its earnings growth halves for the next few years, B2Gold's PEG ratio comes around 0.3 times, which indicates the stock is significantly undervalued and has a big growth potential.

Gold prices will likely march higher again next year. Currencies come under pressure as global economies are printing more and more money, which ultimately lifts the yellow metal.



## Bottom line

No stock valuation tool is perfect and adequate. But analyzing the PEG ratio should be prudent while investing in growth stocks. It will indicate how much premium is really justified for the expected growth.

**CATEGORY**

1. Coronavirus
2. Investing
3. Stocks for Beginners
4. Tech Stocks

**TICKERS GLOBAL**

1. NYSE:SHOP (Shopify Inc.)
2. NYSEMKT:BTG (B2Gold Corp.)
3. TSX:BTO (B2Gold Corp.)
4. TSX:SHOP (Shopify Inc.)

**PARTNER-FEEDS**

1. Business Insider
2. Koyfin
3. Msn

4. Newscred
5. Quote Media
6. Sharewise
7. Yahoo CA

**Category**

1. Coronavirus
2. Investing
3. Stocks for Beginners
4. Tech Stocks

**Date**
2025/08/22
**Date Created**
2020/12/30
**Author**
vinitkularni20