Buy Canada's Top Technology Growth Stock

Description

Constellation Software ([TSX:CSU](#)) is an [iconic Canadian technology firm](#). The company has produced phenomenal returns for shareholders over the last two decades and appears set to continue delivering market-beating returns for the next several decades. Under the leadership of Mark Leonard, Constellation's chief executive officer, who's kept a quiet profile, the company has outperformed most Canadian companies over the long term.

Generally, Constellation prefers to acquire vertical market software (VMS) businesses with several desirable characteristics. The company looks for growing business with a [diversified customer base](#), high relative market share, and capital-constrained competitors. That said, Constellation sometimes acquires VMS businesses with declining revenues, concentrated customer bases, low relative market share, and well-funded competitors. These are more opportunistic in nature, and the company does so when it believes that the correct combination of customer relationship management and market segmentation will lead to attractive returns.

Decentralized management structure

In addition, Constellation's decentralized management structure is key to the company's continued revenue growth. The company has experienced management teams operating in each VMS business, backed by infrastructure at the operating group level and a small corporate head office. The corporate head office provides financial and strategic expertise with respect to capital allocation, acquisitions, finance, tax, and compensation policy, and attempts to identify and share best practices.

Warren Buffett once said, "Show me the incentive and I'll show you the outcome." Constellation has one of the best compensation structures in Canada aligned with the right incentives. Some executives at Constellation, who earn in excess of $75,000 per annum and have bonuses in excess of $10,000 per annum, are required to own the company's shares for a period of up to 10 years. At a minimum, these restrictions require employees to hold shares for the first two years following acquisition.

Right incentive structure

Senior executives are required to invest 75% of their bonus in shares of the company that are subject to the same restrictions on resale for a period of three to 10 years. Once every five years, employees may elect to receive 100% of an individual's bonus in cash. Constellation's bonus plan encourages employees to participate through share ownership in the value that they have created.

Also, the company uses a combination of field sales and inside sales where appropriate. Constellation generally licenses the use of the company's products to customers rather than transferring title to them. These licences contain terms and conditions prohibiting the unauthorized reproduction, disclosure, reverse engineering, or transfer of Constellation's products.

Protection of trade secrets

In addition, Constellation attempt to protect trade secrets and other proprietary information through agreements with suppliers, employees, and consultants. All material components of Constellation's products have been developed by individuals, most of whom have assigned all rights to the company, except for commercially available components.

For fiscal 2020, approximately 44% of Constellation's revenues were transacted in the United States, 12% in Canada, 34% in United Kingdom and Europe, and 10% in the rest of the world. No single customer accounted for more than 1% of Constellation's total revenues in fiscal 2020. This diversity should serve long-term shareholders well.

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