



## Sector Whiplash: 1 Tech Stock (Not Shopify (TSX:SHOP)) Could Survive

### Description

Investors complained about the high valuation and steep share price of **Shopify** ([TSX:SHOP](#)) ([NYSE:SHOP](#)) when it ruled the TSX in 2020 and 2021. In 2022, no one would dare catch the falling knife. But **Constellation Software** ([TSX:CSU](#)) appears to be a better investment prospect than the erstwhile tech superstar.

*BNN Bloomberg* reports that the anxiety level of the members of Canada's [tech sector](#) is rising fast. The selloff is likely to continue with surging inflation and multiple rate hikes. Shopify hasn't reached rock bottom, although the current share price of \$452.54 is 80% lower than its 52-week high of \$2,228.73. On a year-to-date basis, the e-commerce platform is down 74%.

While the nature of the businesses is different, it's worth comparing the earnings potential of each to determine which one could survive the whiplash.

### Manager of exceptional businesses

Constellation Software's industry-specific software businesses provide specialized and mission-critical software solutions globally. The \$40.86 billion company caters to clients, private and public, in Canada, Europe, and the United States. Management's primary objective is to acquire, build, and manage exceptional companies.

Most of the target acquisitions are good mid- to large vertical market software (VMS) companies. They must have consistent earnings and growth, generally revenue growth of at least 20%. Constellation derives revenue from software licence fees, maintenance & other recurring fees, professional service fees, and hardware sales.

In Q1 2022, revenue increased 22% to US\$1.43 billion versus Q1 2021. Net income reached US\$111 million compared to the US\$175 million net loss in the same quarter last year. Notably, free cash flow (FCF) increased 21% year over year to US\$324 million.

According to management, the company has sufficient cash and available credit capacity going

forward. Despite the negative working capital of its VMS businesses, Constellation can continue to grow the business organically without any additional funding.

The slump of Constellation isn't as severe as the perennial TSX30 winner. At \$1,935.08 per share, the year-to-date loss is 17%. The total return in 3.01 years is 78.41% (21.24% CAGR). Shopify's performance deteriorated significantly. In the same period, the overall return is down to 17.68% (5.57% CAGR).

Based on market analysts' forecast, Constellation Software's return potential in one year is between 31% and 60%. Also, the tech stock pays a modest 0.27% dividend.

## Numerous challenges

While total revenue in Q1 2022 increased 21%, the growth is tiny compared to the 110% in Q1 2021 when the company registered its highest revenue growth. In 2020, Shopify also became Canada's largest publicly listed company, unseating **Royal Bank of Canada** from the throne.

Shopify's market cap is down to only \$58.82 billion as against RBC's \$186.76 billion. In the three months ended March 31, 2022, the net loss reached US\$1.5 billion compared to the US\$1.3 billion net income in Q1 2021. Its CFO Amy Shapiro said, "We're operating in a more measured macro environment relative to 2021 moderated by inflation."

The e-commerce industry, in general, will face numerous threats and challenges going forward, including inflation and ongoing supply chain issues.

## More downturns

Many market analysts expect more downturns in the tech sector in the months ahead. It might take time before we see the return of momentous growth that tech companies enjoyed over the past couple of years.

### CATEGORY

1. Investing
2. Tech Stocks

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2. TSX:CSU (Constellation Software Inc.)
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