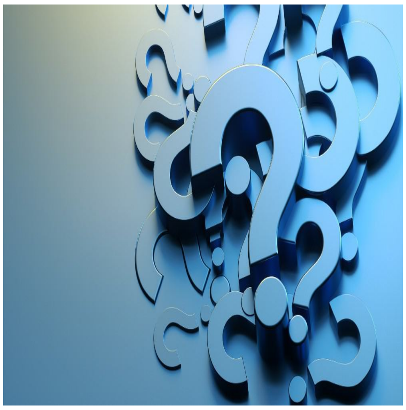

Michael Burry Is Buying Growth Stocks: Should You?

Description

Michael Burry, the hedge fund manager famously portrayed by Christian Bale in *The Big Short,* has been exceptionally active. Burry's fund management company has added several positions in recent months while the manager has been tweeting about his outlook for the market.

Considering Burry's track record, it makes sense to dig into his latest moves. Here's what the investor is betting on and what Canadian investors can learn from it.

Bullwhip effect

In his recent tweet, Burry highlighted the build-up of inventories at retail stores. Retailers seem to have overordered goods due to supply chain delays. However, consumer demand is slowing down because of rising interest rates and inflation. That means retailers could have too much supply and very little demand in the months ahead, which could lead to heavy discounting.

Burry calls this the "bullwhip effect."

Discounting reduces prices and chills inflation, which could convince central banks to pivot on their rate-hiking strategy. In fact, Burry even said the Federal Reserve could *cut* rates in the near term. That could boost the valuation of growth stocks.

This is probably why he added **Alphabet** and **Meta Platforms** to his portfolio in the second quarter of 2022. His investment company Scion Asset Management now holds 6,500 shares of GOOGL and 80,000 shares of META, making them the fourth- and sixth-largest positions in the portfolio, respectively.

Burry isn't alone in this bet. Other noteworthy investors such as Prem Watsa, Bill Miller, and Pat Dorsey also added these stocks to their portfolios. It could be an indication that the tide is turning and growth stocks are due for a rebound.

Growth stocks

Canadian tech and growth stocks could be exposed to the same factors. A dip in inflation and a slowdown in rate hikes could unlock value in some of these beaten-down stocks.

Enterprise tech giant **Constellation Software** (TSX:CSU) could be a target. The stock has lost 20% of its value year to date. But it has held up better than other tech stocks. That's because the company's underlying fundamentals are robust. Constellation is profitable and cash flow positive with a long track record of success. Nearly half of its earnings are derived from government clients, which makes its cash flows more reliable.

In recent months, the Constellation team has ramped up its pace of acquisitions. Snapping up niche software companies at discounted valuations helps the company grow faster. This could be reflected in the company's cash flows in the future.

The company reported US$324 million in free cash flow in its most recent quarter. That's roughly $1.67 billion in annual free cash flow. Meanwhile, the company's market capitalization is $40 billion, which implies a price–to-free cash flow ratio of 24. Put simply, Constellation Software is undervalued.

If the bullwhip effect kicks in as Michael Burry predicts, growing tech stocks like Constellation could see higher valuations soon. Investors should keep an eye on this opportunity to make a contrarian bet before the rest of the market catches up.

CATEGORY

1. Investing

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