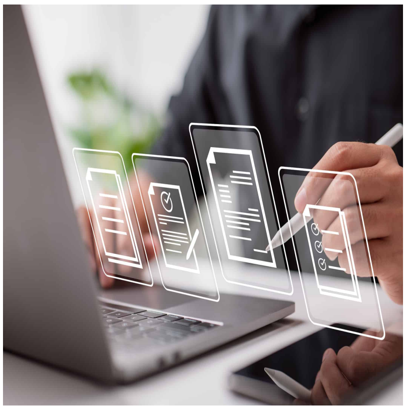

# Why I Think Constellation Software (TSX:CSU) Stock Has Market-Beating Potential

### Description

Canadian tech giant **Constellation Software** (TSX:CSU) is probably the most underrated stock on the market. The company has steadily expanded its footprint over several years by flawlessly executing a growth-via-acquisition strategy.



In 2022, I believe the stock is perfectly positioned for market-beating returns. Here's why Constellation Software could be an outperformer over the coming years.

## Strong U.S. dollar

Constellation Software is a global software conglomerate. That means it owns small, niche software companies across the world. However, the majority of its business is based in the United States. That's why 50% of its revenue in the first half of this year was derived in U.S. dollars.

The dollar has been exceptionally strong this year. Every other currency (including the British pound, euro, and Canadian dollar) has lost value against it. If this trend continues, Constellation could see further upside in its earnings.

## Government contracts

Nearly half of the company's software clients are government agencies. This makes subscription revenue much more consistent and reliable. Government clients are not exposed to the same market forces as their commercial counterparts. That means a recession won't impact their software budget.

Even for commercial clients, essential software tools are less prone to cost-cutting measures. If a recession hits next year, I believe Constellation's clients would be more likely to cut rental or staffing costs before unsubscribing from mission-critical software packages.

## Acquisition valuations

The tech industry has been at the epicentre of the ongoing bear market. Tech stocks have lost more value than most other industries this year. This pain is flooding over into private valuations as well. Venture capitalists and angel investors have pulled back, which has pushed private software valuations lower.

The environment is perfect for strategic buyers like Constellation Software. Indeed, the company has deployed over $1 billion for acquisitions in the first half of this year. That's more than it did in all of 2021. I expect this pace of buyouts to continue, as valuations remain suppressed.

Acquisitions completed this year may be fully reflected in Constellation's earnings in the years ahead. That should help push the parent company's valuation higher.

## Valuation

Constellation Software stock is down 16% year to date. That's despite the fact that the company's sales and earnings have been expanding this year. In its most recent quarter, Constellation reported 30% revenue growth and 43% net income growth.



Better fundamentals and lower stock price make the stock cheaper. Constellation stock is trading at an enterprise value-to-revenue ratio of 4.5. This ratio was consistently above five since 2019. It's also trading at a price-to-earnings ratio of 25.8, when it was consistently above 30 since 2019.

If Constellation's recent acquisitions are as successful as its historic ones, and the valuation reverts to mean, the stock could outperform. That's why I'm betting on Constellation stock for the foreseeable future.

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