Should You Buy Shopify Inc.?

Description

In case you haven't heard, **Shopify Inc.** (TSX:SH)(NYSE:SHOP) is the newest tech darling available to investors, having gone public earlier this week.

The Ottawa-based company targeted a price of US$12-14 per share. Demand was so high that the offering price was raised twice, settling at US$17 per share. But even at that price, demand was far higher than supply. As of this writing, one Shopify share will cost you roughly US$30.

So, what's so special about this company? And more importantly, should you own a piece? Below we take a look.

Spectacular growth

Shopify "provides a leading cloud-based commerce platform designed for small and medium-sized businesses," as it states in its prospectus. In plain English, it provides a very easy solution for small companies to sell their product online. In fact, the company claims that merchants can set up their Shopify-enabled shops in as little as 15 minutes.

The company has been very successful thus far, and is growing at light speed. In 2013 revenue doubled from the previous year, and in 2014 revenue doubled again. The rapid growth has continued in 2015, with US$37.3 million in revenue, up 98% year over year.

Thus far, the company still doesn't generate a profit, but this is normal for a fast-growing tech company. Growth is clearly the number one priority, as it should be.

An expensive stock

At this point, everything is going right for Shopify, so one would expect the shares to be pricey. But at US$30 per share, one has to wonder if there's any upside left.

At this price, Shopify is valued at roughly US$2.2 billion. This is for a company with about 160,000 customers, generating US$1,000 in annualized revenue apiece. This works out to an eye-watering 14 times revenue, for a company that still doesn’t generate profits.

Let’s put that in perspective. Suppose Shopify grows at 70% per year for three years. Then it makes a 10% profit margin. Then it trades at 30 times earnings. For practically any other stock, this would be a dream scenario. Yet if this happened with Shopify, the stock price would decrease by about 10%.

What should you do?

For a company such as this, there’s still tremendous upside, especially if the company is able to sustain its growth rate for many years. Using the example above, if Shopify grows at 70% for five years instead of three, and all other assumptions are kept the same, then shareholders will make 160% on your money (that works out to more than 20% per year). And if Shopify keeps doubling its revenue every year, there’s even more upside.

So, should you jump in? Well, that depends on what kind of investor you are. If you’re entering retirement, and looking to protect your money, then you should opt for stable dividends instead. But if you like to take chances, and have some extra money to dabble with, then by all means, this will be a fun stock to own.

CATEGORY

1. Investing
2. Tech Stocks

TICKERS GLOBAL

1. NYSE:SHOP (Shopify Inc.)

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