



Shopify Inc.: Shop Till You Drop?

Description

Shopify Inc. ([TSX:SHOP](#))([NYSE:SHOP](#)) has been on a fantastic run lately. The stock is up over 60% this year, but it has since seen its momentum flatline around the \$56 level. The company reported a fantastic third quarter that crushed analyst expectations, but is the stock too overvalued to have any upside going into the new year?

Shopify is an e-commerce company that develops a software-as-a-service model for online stores. The company currently has over 300,000 merchants, and this number is growing at a ridiculous rate.

Although Shopify is growing very fast, it's surprisingly more predictable than your typical high-flying tech stock. Shopify makes its revenues through subscription fees, and as long as its merchants love the product, they will continue to use the platform, and more subscriptions will come flowing in from other merchants looking to make the jump to Shopify's platform.

The business model is relatively easy to understand, and this is what Warren Buffett and his followers love about businesses. Although Warren Buffett is not a huge fan of tech stocks, Shopify might be a company he would consider because it's simple to understand how the company will grow its earnings over the long term.

Shopify gets its cash flow in a similar fashion to how telecoms collect their steady stream of cash flow from their wireless network users. Is Shopify's subscription base as stable as a typical telecom? Most definitely not. The telecoms tie their customers to contracts that last up to two years. There's also gigantic moats that prevent their subscriber base from jumping ship.

Shopify doesn't have such a moat, so the company will have to continuously make its platform better and easier to use by investing a big chunk of its cash back into R&D. Technology changes fast, and there are no barriers to entry, but I believe the management team at Shopify is very capable of innovating its platform down the road to offer an attractive service that its subscribers will not be able to drop.

I don't believe Shopify needs to lock down its subscribers. It offers monthly plans, and usually the users of these plans come back for more because they enjoy the experience of using the platform.

They could switch to a competitor, but they stick with Shopify by choice. As a result, the platform has become very popular among merchants and continues to gain more subscribers each quarter.

The company is definitely one of the few great tech names in Canada, but is the stock a buy at current prices?

The stock is quite pricey right now, and I would wait for a pullback if there is one. Impressive quarters are pretty much expected as we head into 2017, and if there's a slight miss, we could see the stock pull back a great deal, as momentum traders start losing faith in the stock.

The stock trades at a nine price-to-book multiple and a 10.2 price-to-sales multiple. The stock isn't cheap, and it appears that there's very little upside for next year. I'd stick on the sidelines for now, but I'm definitely keeping this fantastic name on my radar.

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Date

2025/09/20

Date Created

2016/12/27

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