Shopify Inc. Gets Downgraded: Here's What You Should Do

Description

Shopify Inc. (TSX:SHOP)(NYSE:SHOP), the e-commerce software as a service (SaaS) provider, has been touted as the next big tech company to watch out for ever since its initial public offering in mid-2015. And with good reason, too — Shopify's e-commerce platform is already attracting small- and medium-sized business merchants in hordes, as the 50% surge in the number of its net new merchants in FY 2016 reflects.

It's interesting, then, that RBC Capital Markets downgraded Shopify stock last week, despite the company's torrid growth. Does RBC Capital know something that investors don't?

Why the downgrade?

RBC Capital downgraded Shopify to "sector perform" from "outperform" but retained its price objective of US$77 on the stock — just about a dollar away from current price.

RBC Capital anticipates a slowdown in Shopify's merchant additions. While the total merchant base is expected to continue growing, RBC believes that Shopify's net additions could decelerate this year and could turn negative by 2018. That means Shopify's immediate growth potential appears to be already factored in to its share price.

Shopify's shares have surged nearly 200% since going public, piling on as much as 80% year to date. Having raised the bar of expectations so high, Shopify must deliver for the stock to maintain momentum.

Does that mean it is time for you to exit Shopify? Maybe not.

On a solid growth trajectory

Even if Shopify is unable to sustain its growth trajectory in the near term, that does not negate its long-term growth potential. Remember how critics sounded the warning bell on **Amazon.com, Inc.** (NASDAQ:AMZN) during its initial years? If you'd bought the Amazon IPO, you'd be sitting on returns above 56,000% today.

Of course, I'm not predicting an Amazon rerun with Shopify, but it has a fundamentally sound business model with a growing list of merchants. Its gross merchandise volume, which reflects the total dollar value of orders processed on the company's platform, surged 99% in FY 2016. Currently, 68% of Shopify's total merchant base is using Shopify Payments, its in-house payment gateway. The company even launched its own credit card reader last month, foraying into the hardware side of the payments-processing business.

The big Amazon boost

Three acquisitions and partnerships with leading-industry players, the most prominent one being Amazon, are bigger highlights. Shopify made its "Sell on Amazon" platform available in December 2016, connecting merchants to Amazon's worldwide customer base. It also roped in **Facebook** Messenger as a new sales channel and has both the U.S. Postal Service and Canada Post as shipping partners.

Expect volatility, but stay put

Clearly, Shopify is a young, growing company that has rightly caught investors' attention. This week is crucial for investors as the company will report its first-quarter earnings on May 2. It expects to generate revenues between US$120 and US$122 million, representing 65-68% year-over-year growth. Breaking even could take time, and Shopify shares could be volatile. As long as you can stomach it, there's no reason to sell your shares.

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