



## Shopify Inc.: 1 Scary Long-Term Risk That Nobody Is Talking About

### Description

**Shopify Inc.** ([TSX:SHOP](#))([NYSE:SHOP](#)) is arguably Canada's hottest stock right now. It's a high-flying tech stock that many call the Canadian **Amazon.com, Inc.** Shares have skyrocketed over a short period, and there's nothing but optimism in the headlines.

I think Shopify is a great business with a wonderful product. Subscriber growth is off the charts, but valuations are getting ridiculous, and everyone appears to be greedy. Does that mean you should be fearful? Possibly.

Here's the one issue that makes me afraid to own shares at such an inflated price.

### **Merchants love Shopify, but what if they can't stay in business over the long term?**

The R&D team keeps finding new ways to make the lives of its merchants easier. That keeps them happy, and they're going to stick around for the long haul if all goes according to plan. Customer loyalty is great, but there's one major issue with providing software as a service to small- or medium-sized businesses: the probability of these businesses failing is high as time progresses!

Think about it. You're starting a new business, and you use Shopify. You love it, and the experience is great, but you find that sales are slowing and you're eating into your savings. You shrug it off and tell yourself that you'll make a profit eventually once you invest more money. Fast forward a few years later, you can no longer afford to keep your business running; sadly, you need to shut down operations and cancel your Shopify subscription.

That's the sad reality of small businesses. A lot of the time, it just doesn't work out.

According to the U.S. Bureau of Labour Statistics, "About half of all new establishments survive five years or more and about one-third survive 10 years or more. As one would expect, the probability of survival increases with a firm's age. Survival rates have changed little over time." That's some food for thought for investors.

## **Shopify is gaining subscribers, but will two-thirds of its subscriber base go out of business a decade from now?**

It's expected that over the course of the long term, subscribers will be lost because their businesses simply won't survive. It's unfortunate news about being a service provider to smaller-sized businesses. Shopify's subscriber-growth momentum is likely to continue to accelerate, and, as of now, it appears that no peak is in sight.

But when a peak is eventually reached and subscriber growth slows (who knows when this may be), investors may want to start trimming their positions since subscriber losses could become a problem, and not because Shopify's platform isn't one of the best in the market.

### **Shopify could be in for a plunge once the next recession arrives**

Once the next recession happens, the lives of small-business owners will be that much harder, and it'll truly be a fight for survival. If the next recession is a nasty one, it's likely that more small businesses will go belly up, and that means a significant amount of subscriber losses for Shopify.

Shopify knows that, ultimately, its success depends on the success of the small businesses that subscribe to it. If a business can't afford to keep operations running, then the subscription goes out the window. Customer loyalty won't mean anything then!

That's why Shopify has been investing in additional tools and add-on services for specific businesses to help them succeed and lower the probability of failure. Shopify can collect additional fees for its these tools, so it's a win-win for Shopify and its merchants.

Shopify doesn't want to lock in merchants to long-term contracts because the probability of contract breaches could be high, especially for businesses that fail fast. It's clear that Shopify wants to be a friend of the merchant — not a long-term obligation to worry about.

### **Bottom line**

Don't get me wrong. Shopify is a fantastic business, and I believe subscriber growth is just getting started, but the easy money has been made. If you want to bet on Shopify near the \$130 levels, you should know the long-term risks.

Shares pretty much have nothing but optimism baked in right now, and I find that a lot of investors dismiss the potential impact of a major economic downturn.

If you're still bullish on Shopify, but you want to reduce your risk, consider picking up shares in small chunks on any dips that may happen going forward.

Stay smart. Stay hungry. Stay Foolish.

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