Better Momentum Stock: Shopify Inc. or Dollarama Inc.?

Description

Shopify Inc. (TSX:SHOP)(NYSE:SHOP) and **Dollarama Inc.** (TSX:DOL) are two incredible momentum stocks that can't be slowed down. Shares of both companies have taken a few breathers here and there, but they always find a way to make up for lost time by breaking out shortly after. Both companies are explosive growth kings with promising long-term prospects, but the valuations are questionable.

So, does it make sense to own shares of these companies for the long term? Or could a much better entry point be on the horizon for either stock?

Both Shopify and Dollarama are momentum-trader favourites, but if you're a long-term investor who's got value on your mind, is it a risky proposition to own shares of such companies that keep finding ways to surge to all-time highs? I believe there's less of a margin of safety involved with buying shares of either company after their tremendous runs, but that doesn't mean there's little upside remaining. On the contrary; there's probably a tonne of upside that investors could realize over the long term. However, with such inflated valuations, short- to medium-term corrections are still a possibility, so investors should not get too euphoric on the momentum by loading up on shares all at once.

If you're looking for a way to get some skin in the game without taking on too much additional risk, then it's probably a prudent strategy to buy shares in small increments over time. And if shares of either company plummet, you should be cheering and buying more on such dips.

Both companies have seen insane share price appreciation, but it's important to note the differences between the two companies.

Shopify is a high-flying e-commerce play that is gaining subscribers at a ridiculous rate. The company is not profitable yet, but it'll soon reach that point, and if subscriber growth continues to pick up, it's likely that shares could continue to appreciate at the rate we've seen in the past.

While Shopify has an impressive platform aimed at small- and medium-sized businesses, I believe shares have run way ahead of reality and an investment in the high $130 levels is somewhat speculative. There are huge rewards, but the risks are also of a similar magnitude.

Dollarama has grown its EPS at an astounding rate over the last few years, and there's still a tonne of room to run as the company consolidates a very fragmented industry. The company continues to find ways to improve its gross margins and has had tremendous success with its multi-pricing strategy.

The stock of DOL has a premium 34.8 price-to-earnings multiple because of the company's solid EPS growth expectations and its recession-resistant nature. I believe both traits deserve a premium valuation; however, a P/E near 35 is really pushing it.

Bottom line

These two momentum stocks could generate huge gains in a short amount of time, but it's important to understand the risks associated.

SHOP and DOL are too expensive for my liking, but if you're keen on riding the euphoria that these two momentum stocks could offer, then you should accumulate incrementally with time, but only if you're in it for the long term. Be patient and build your position over time, while you profit without taking on too much risk!

If I had to choose one, I'd probably go with Dollarama because of its defensive nature, which will come in handy once the next economic downturn arrives! Dollarama is also a simpler, easier to understand business, which probably won't see major changes to its business model over the course of the next decade.

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