Shopify Inc.: Buy the Dip or Wait?

Description

Shopify Inc. (TSX:SHOP)(NYSE:SHOP) is under attack, and investors are wondering if the recent pullback in the stock is a signal to book profits or an opportunity to load up on more shares.

Let's take a look at the current situation to see if the Canadian company deserves to be in your portfolio today.

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Bad press

Shopify took a hit in recent days after a well-known short seller, Citron Research, announced it was shorting the popular e-commerce company's stock.

If you are unfamiliar with the business, Shopify is essentially a one-stop shop for small- to medium-sized business owners who want to set up an online store to sell their products.

Through its subscription plan, the company makes it affordable for merchants to get up and running in very little time, providing both the online platform, as well as payment systems and inventory management services.

Citron's founder, Andrew Left, didn't hold back in his criticism of Shopify when he revealed his reasons for betting against the stock.

Left called Shopify a "get-rich-quick" scheme and claimed Shopify violates U.S. Federal Trade Commission rules, citing marketing material on Shopify's website. In addition, Left criticized the company's affiliate program, which pays commissions to third-party partners who refer new merchants to Shopify.

Is Shopify's stock expensive?

At the time of writing, Shopify trades for $122 per share, which gives it a market capitalization of about $12 billion.

Shopify reported a net loss of $14 million in the second quarter. Revenue for Q2 2017 came in at $152 million, so the stock trades for about 20 times revenue on an annualized basis.

At that kind of valuation, investors have to be convinced the recent growth is set to continue, and the company will eventually be profitable. Revenue grew 75% on a year-over-year basis in the quarter, which suggests the upward momentum is certainly strong.

Should you buy?

The stock is down from $150 per share, but it’s still up more than 100% in 2017. When we see gains of this magnitude, there is always a risk that investors who got in at much lower prices could start locking in their profits, especially if they think the run is done.

On top of that, more volatility should be expected in the near term, as the market tries to figure out whether or not Citron’s claims are valid.

However, the long-term outlook for Shopify should be solid. Citron even said in its online report that it thinks Shopify’s technology is “the best build-your-own e-commerce software on the market.”

If you can handle the volatility, it might be worthwhile to add a small position on further weakness, but I wouldn’t back up the truck today.

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