Shopify Inc.: Why Shareholders Have the Right to Be Worried

Description

Shopify Inc. (TSX:SHOP)(NYSE:SHOP) plunged 7.03% in a single trading session, and the entire tech sector sold off. Tech names have been top performers over the past year, but as investors gradually begin to move their capital to non-tech names, it may be time to finally part ways with Shopify — a company that still has many uncertainties in its future, which have likely caused shares to essentially flat-line since May.

Overexposed to Shopify? You're probably not alone

Industry-wide sell-offs happen, even though tech investors may have forgotten what it's like. Another tech burst probably isn't in the cards, but it's a huge wake-up call to investors whose portfolios aren't properly diversified across various industries. The tech-heavy Nasdaq 100 index plunged nearly 2%, while other diversified indices actually held up, with the Dow actually rising by a fair amount.

It's tough to diversify, especially as a Canadian investor; our options are limited with the low loonie relative to the U.S. dollar. It's not a mystery that Canada doesn't have much in the way of tech stocks, so investors who feel more comfortable investing at home may be opting for the small basket of tech offerings that the TSX has to offer.

When it comes to Canada's tech basket, there isn't much compared to our neighbours south of the border. When it comes to Canadian tech, it's hard to steer clear of Shopify, which has been the hottest tech play that Canada has had in years. Shopify is an incredibly innovative company in one of the fastest-emerging sectors (e-commerce) out there, so it's not a surprise that even U.S. investors have been attracted to the stock.

Tech is an essential part of a portfolio, and to many Canadians who are not interested in venturing into the U.S., the only real option is Shopify. It's a compelling business, but there are many issues that may stop the stock from flying higher in the near term.

You're probably aware of Andrew Left's short position and the reasons he's short the stock. While there are many far-fetched claims in his short report, there are a number of concerning issues that should be ringing alarm bells in the ears of shareholders. Even before Left publicly announced his short position, I'd pointed out that the company's churn rate and overvaluation were reasons to sell the stock.

Betting against Andrew Left could lead to trouble

Left has allegations of illegal activities (I think the company is operating legitimately), and he wants the FTC to get involved. He's probably collecting more evidence for his case as you read this article, which could lead to another short report in the near future.

He's an opportunist, so should Shopify take another meaningful dip, he may choose to release another report to exacerbate the fear of shareholders. If Left manages to get the FTC to investigate Shopify, I suspect the stock could receive yet another "Left hook" to the chin, and this time, shares may not be so quick to get back on their feet.

Bottom line

There's no question that Shopify is a terrific product with a promising growth runway, but subscriber churn and overvaluation should be reason enough to sell the stock. And with Andrew Left doing everything in his power to drive the stock down, I wouldn't feel comfortable recommending shares, as they continue to fluctuate around the $130 level. They're stuck in limbo right now, so a break-out is going to be tough from here, especially since investors may be poised to dump their extremely overvalued tech stocks as a part of a broader tech market sell-off.

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