Shopify Inc.: Will the Stock Take Off in 2018?

Description

Despite short-seller allegations and a lengthy period of stock price consolidation, **Shopify Inc.** (TSX:SHOP)(NYSE:SHOP) still managed to surge ~100% in 2017. As we head into the latter part of 2018, the million-dollar question is whether the stock will be able to shake off Andrew Left's claims and regain the momentum it demonstrated prior to spring of 2017. While many points of Andrew Left's short report may be far-fetched, investors need some answers before the stock can truly skyrocket to the next level.

Longer-term churn rates are still a red flag

One major concern that I've had with Shopify is the potential for accelerating churn rates and a lack of transparency when it comes to the quality of Shopify's merchant base. When it comes to Shopify's non-plus merchants, it's difficult to quantify the number of lower quality merchants or subscribers who are more likely to ditch their subscriptions over the very short term. This type of information is extremely important when you consider that such merchants aren't locked into long-term contracts.

Of Shopify's non-plus offerings, there's the Lite Shopify, Basic Shopify, Shopify, and Advanced Shopify, which go for $9, $29, $79, and $299 per month, respectively. One could argue that each tier represents the quality of a merchant, but that picture isn't entirely accurate. For example, a merchant who desires third-party calculated shipping rates will have no choice but to choose Shopify Advanced for this exclusive feature, which tells us nothing about the quality of the merchant.

While monthly recurring revenue (MRR) may be surging, it's important to remember that a huge chunk of Shopify's overall merchant base may be of very low quality. They are thus more likely to ditch their memberships on a whim versus the higher quality merchants whose businesses are fundamentally sound.

Unlike contracted revenue streams, Shopify's MRR is subject to a ridiculous amount of volatility, which will become more apparent once economic conditions become harsh. In addition, we must remember that most startups are destined to fail, which leaves a huge portion of Shopify's MRR at risk once the next recession shows its ugly head. Even without a recession, the failure rate of a startup increases as time progresses, which means we could witness a large percentage of Shopify's merchant-base evaporate with zero warning in a few years.

Shares are priced for perfection

Shopify is a red-hot e-commerce growth player that's poised to benefit from the mass digitization of SMB retailers; however, the price you'll pay today, with shares at the $140 levels, is absolutely ridiculous. Shares currently trade at a whopping 18 times the sales! I challenge you to find a compelling stock that's trading at a larger price-to-sales multiple. Shopify is now one of the most expensive stocks, not only on the TSX, but also in North America.

Bottom line

Shopify isn't a very predictable stock, and it's absurdly overvalued. Therefore, based on the principles of Warren Buffett, you should avoid this stock like the plague. However, given the general public's affinity for high-growth, speculative plays of late (Bitcoin, marijuana), I think Shopify will move higher in 2018.

Unless you're comfortable with placing a speculative bet, I wouldn't advise buying Shopify, at least, not until shares drop to the $100 levels.

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