

Shopify Inc.: Don't Miss This Great Tech Stock

Description

Reader know I am a big fan of **Shopify Inc.** (<u>TSX:SHOP</u>)(<u>NYSE:SHOP</u>). I've gone so far as to suggest that Shopify could be <u>Canada's top tech stock</u>. I believe that because Shopify has a unique network effect that, as time goes on, gives it even more reach and influence.

It all comes down to its business model. As a Software-as-a-Solution (SaaS) company, it derives it revenue from subscription fees. Users spend anywhere from US\$29 to US\$299 per month for their shops — though there is a growing number of large-scale brands coming online, paying US\$2,000 or more per month.

What stands out about the model is that revenue compounds. In month one, a company with this model can sign up 1,000 people at US\$29 per month, resulting in monthly recurring revenue (MRR) of US\$29,000 after the first month. In month two, another 1,000 people sign up at US\$29 per month. Now the MRR is US\$58,000. In the third month, it's US\$87,000, and so on.

According to Shopify's investor deck, in Q1 2012, it had an MRR of US\$1.1 million. In Q3 2017, its MRR was US\$29.9 million. That's a CAGR of 77%.

But let's go back to that network effect. Shopify found that it could generate consistent revenue from its SaaS business and generate incremental revenue from other services. For example, rather than needing to procure a credit card processor or a shipping solution, you do it all in the Shopify platform. As more goods are sold through Shopify stores, Shopify earns more money.

The numbers show it. In 2012, the Shopify network had US\$700 billion in gross merchandise volume. In 2017, it had US\$26.3 billion. That results in more revenue being derived from these additional services than the SaaS model. In 2017, the company brought in US\$673.3 million in revenue with more than half coming from its merchant solutions business, not its subscription business.

There are some bits of news that have come out over the past few days.

First, it was reported that the Ontario Cannabis Retail Corporation will use Shopify's online platform and its point-of-sale software for all marijuana purchases. This could be a big play for Shopify, but we

don't yet know how much recreational marijuana activity there will be in the province.

Second, Shopify announced that it was issuing 4,800,000 Class A shares at a price of US\$137, so it can raise US\$657,600,000. Any time there's a new raise, investors get frustrated because it dilutes their ownership stake. But the cash will be reinvested into the company, so it can continue its growth.

There is no denying that Shopify has the potential to grow a lot more. The small- to medium-sized business addressable market is US\$64 billion, and Shopify has not even reached 20% of that. As it continues to expand, form new partnerships, and add new services, the compounding revenue numbers will only get higher.

But like any growth stock, there will be turbulence. If you're looking for a safer ride, there are other opportunities in the market.

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2025/07/20 **Date Created** 2018/02/23 Author jaycodon

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