



Shopify Inc. May Be Too Hot to Handle at \$200+

Description

Despite multiple attacks from the infamous activist short-seller Andrew Left, **Shopify Inc.** ([TSX:SHOP](#))([NYSE:SHOP](#)) stock managed to rally 77% over the past year as investors move past Mr. Left's seemingly "baseless" allegations of wrongdoing. Mr. Left's attempts at bringing the stock down did manage to spark a surge in volatility, however; the uptrend still remains as investors remain euphoric over the rise of the entrepreneurial economy.

With an industry-leading platform catering to small and medium-sized businesses (SMBs), management is committed to leveraging innovative new technologies like artificial intelligence (AI) and augmented reality (AR) in order to win over new clients while simultaneously lowering attrition rates with its existing merchant-base.

Despite Shopify's continuously improving interface and an acceleration of optional merchant solution offerings, there are many concerns that go beyond the points that Mr. Left shed light on in his report. Not only is the [valuation](#) out-of-this-world (over 21 times sales and 17 times book), but there are far too many uncertainties to be able to form a sound long-term investment thesis.

Subscriber churn remains a major question mark and its robustness may be tested come economic hardships. Given the [high bankruptcy rate for small businesses](#) within the first few years of their lives, Shopify stock stands to be completely obliterated come the next economic downturn, when its merchants will be unable to afford to continue operations at a time when consumer spending falls off a cliff.

Given that there's no way to accurately quantify the proportion of low-quality "drop shipping" merchants that resell counterfeit products from foreign countries, it's difficult to gauge exactly how Shopify's subscriber-base will fare once times get tough. I suspect that most of Shopify's lower-quality merchants (like drop shippers) will dump their subscriptions on a whim on the first signs of a peaking business cycle. The whole business of drop shipping has shady margins and would therefore not be very economical as demand for cheap imports plunge.

Bottom line

As one of the few high-flying e-commerce plays on the TSX, there's a massive scarcity premium attached to shares, although the long-term growth prospects may seem worthy of an inflated multiple. There are far too many unknowns, making it difficult to justify paying an exorbitant multiple for a company that may have a difficult time navigating economic downturns. As it stands, I believe the risk/reward trade-off is just not worth it for the average growth investor.

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