Is it Time to Invest in Shopify Inc. (TSX:SHOP)?

Description

Shopify Inc. (TSX:SHOP)(NYSE:SHOP) has been an investor darling for some time now, rising from $117 one year ago to over $228 today — an almost double.

But looking ahead, the stock is looking too risky on a number of fronts.

Earnings surprise

Adjusted earnings have handily beat expectations in the last three quarters. That's positive.

Growth in monthly recurring revenue was 57% last quarter and compares to a growth rate of over 60% in the first quarter last year — also positive.

But I still have lingering concerns that make this stock a risky proposition at best.

We still lack visibility with regard to merchant disclosure, and the churn rate continues to be an issue, as Shopify continues to have small, higher-risk companies that make up a significant proportion of its customers.

And although merchant additions have been strong in the last two years, with the company seeing strong merchant additions of 232,000 in 2017 and 134,000 additions in 2016, the first quarter of 2018 saw a drop off of this number.

Marijuana industry has sent shares higher

Shopify has made significant traction in the marijuana industry, and with online sales expected to ramp up as the year progresses, Shopify would seem to be a good way to gain exposure to this industry.

And with the company inking a deal with **Aurora Cannabis** for the building of an online cannabis platform, the company is further solidifying its place in the industry.

This follows the announcement earlier this year that the Ontario government will use Shopify's e-commerce platform, and it gives further validation of the company's offering.

But beyond this, there are issues.

Valuation

A look at Shopify, or any other stock, for that matter, is not complete without looking at its valuation.

The valuation is clearly still very lofty, as the stock has defied gravity and continues to rise, with a three-month return of 31%. The stock's P/E multiple on 2020 consensus earnings expectations is almost 200 times.

Eventually, the market will begin to value these shares off of earnings multiples. With the company posting adjusted EPS of $0.05 in the latest quarter, the market will increasingly shift to valuing the stock on a P/E basis.

While recurring revenue is increasing, the stock's valuation is pricing in much of the good news in the short to medium term, and upcoming headwinds will serve to drive the valuation down — headwinds such as the necessary costs to fund the growth of the business and their impact on margins and future profitability.

In short, your hard-earned money would be better off elsewhere, at least for now.

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