Can Shopify Inc (TSX:SHOP) Crush It With Brick and Mortar Stores?

Description

The year 2018 has been a big one for **Shopify Inc** (TSX:SHOP)(NYSE:SHOP). Between continued (if slowing) revenue growth, a big boost from cannabis and a $500 million investment in Toronto's hottest new office space, the company has been getting some serious press recently.

The latest news?

The ecommerce giant is now opening brick and mortar stores.

In a move that surprised many, Shopify opened its first retail store in Los Angeles last week. The store, which is located in a cluster of boutique shops known as Row DTLA, stocks a number of products ranging from its own point-of-sale hardware to items from Kylie Cosmetics. The move is an unorthodox one for Shopify, which has to date earned most of its revenue from vendor subscriptions rather than direct sales. But depending on how it plays out, it could actually reward investors handsomely.

Rationale for opening stores

In a statement, Shopify COO Harley Finkelstein hinted that the Los Angeles store was about supporting entrepreneurs.

"With Shopify LA we wanted to create a hub where business owners can find support, inspiration, and community" he said. He added, "*Entrepreneurs at all stages and of all sizes can learn together, have first access to our newest products, and propel their entrepreneurial dreams."* Product development VP Satish Kanwar echoed the sentiment, calling the store a hub for entrepreneurs to find *"support, inspiration and community."*

This all sounds fine and dandy. The question is, will it actually drive more sales? A single retail location in Los Angeles will most likely not propel statistically significant sales growth for the company. However, if the idea catches on in more locations, it could help sell more of Shopify's point-of-sale products and perhaps move some offerings by Shopify's partner vendors.

Online sales growing steadily

With or without physical stores, Shopify's sales are already growing at a steady clip. In the most recent quarter, they were up about 62% year-over-year–far head of the TSX average. This is a high growth rate, but it's down from the 68% growth the company was seeing a year prior. The slowing growth rate has been cited as a concern for a company that, as of October 2018, has not yet posted positive earnings.

Earnings

Earnings have been a sore spot for Shopify, whose losses have been growing each quarter since it went public in 2015. In the most recent quarter, its net income was $-23 million, down from $-15 million in March. It's normal for high growth tech companies just three years out from their IPO to lose money, but growing losses like this are a concern. Especially since, in Shopify's case, costs are growing about as quickly as revenue is.

Bottom line

It's not clear exactly how Shopify's new retail location will benefit shareholders. While the idea behind it is sound, it remains to be seen whether it will drive enough sales to make an impact on the company's earnings. Even without retail stores, Shopify is a fast-growing company that's set to get a nice sales injection from legal cannabis. But defensive investors will want to keep an eye on the next income statement before jumping in, as spiralling costs are a concern for this stock.

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