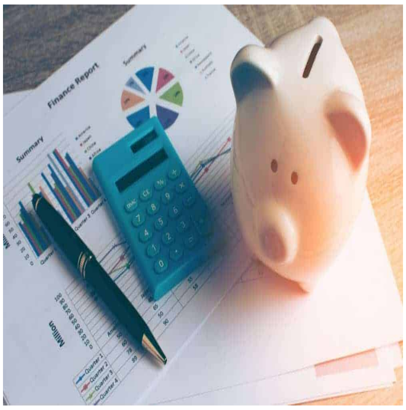

Is Shopify Inc (TSX:SHOP) Stock a Buy After Q3 Earnings Surprise?

Description

This week has witnessed plenty of bad news in the markets. But don't tell that to **Shopify Inc** (TSX:SHOP)(NYSE:SHOP), which just recently had some major good news on the earnings front. Although the company's net earnings were down 20% year-over-year, they beat analyst expectations by a country mile, coming in at $0.04 compared to the -$0.04 expected by Zacks Equity Research.

The relatively strong showing by Shopify in Q3 may have been driven in part by new subscriptions attributable to cannabis sales. A number of cannabis vendors–including both producers and provincially-operated cannabis stores–signed up for Shopify to handle their online sales.

This may help explain how the company was able to grow in Q3 despite the persistent issues in many other sectors. Nevertheless, Shopify's Q3 report contains some areas of concern as well. We can start by looking at revenue growth.

Revenue Growth

Shopify's revenue grew at 58% year-over-year in Q3. This is strong growth; however, the rate of growth is down from 62% in Q2. Declining revenue growth has been cited as a concern for Shopify, which has only been a publicly traded company for about three years. The declining growth rate is especially concerning when compared to the company's accelerating expenses, as we'll see below.

Earnings

In Q3, Shopify posted adjusted net income of $4.5 million, which works out to about $0.04 per share. This surprised many analysts, who were expecting the company to lose money after investing $500 million in Toronto office space. It should be noted that the $4.5 million adjusted earnings is down from $5 million this quarter last year. This is more a testament to rising costs than a lack of growth, however, as the company is still growing revenue in the high double digits.

Operating loss widens

Now for the bad news:

In terms of operating income, Shopify is still losing money–and the loss is getting bigger. The company's Q3 operating loss was $31.4 million, or 12% of revenue, up from $12.7 million in Q3 2017. The operating loss is up both in aggregate and as a percentage of revenue, suggesting that Shopify is having trouble controlling its spending. The company's recent $500 million spending spree on Toronto office space raises particularly loud alarm bells in this regard.

Can it survive TSX index weakness?

Overall, Shopify's Q3 results paint a mixed picture. On one hand, the company is beating analyst estimates and posting positive adjusted earnings. On the other hand, the company still isn't profitable in terms of its core operations; the increase in adjusted earnings mainly came from an increase in the value of marketable securities. Shopify will therefore need to get its spiralling costs under control if it hopes to thrive in the midst of the broader TSX weakness we're witnessing now.

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