Why Shopify Inc (TSX:SHOP) Stock Fell 24% Last Month

Description

Shopify Inc (TSX:SHOP)(NYSE:SHOP) may well be Canada's favourite tech stock. With 1,000,000 active users, 600,000 vendors and $82 billion in total sales, it's easily one of the most successful ecommerce startups in history. It's also doing very well in the markets; year-to-date, it's up about 34%.

But last month, Shopify's stock went on a massive losing streak, shedding about 24% of its value in just a few weeks. It has since recovered, but the volatility has some investors wondering if Shopify is still the great play it once was.

Overall, last month's slide is consistent with Shopify's recent pattern, which is one of dramatic ups and downs. Still, a 24% selloff, when the TSX lost only 7.5% in the same period, is scary to witness. To understand why this sell-off happened, we need to look into some events that influenced the price. We can start with one of the most obvious: insiders selling shares.

Big investors selling

Some big Shopify shareholders have been reducing their holdings recently. This month, I covered two of them: a board member and a major investment bank, the latter of whom reduced their stake by about 9%. Neither of these holders cashed out of Shopify completely, but they did reduce their holdings.

When a big enough shareholder cuts their holdings by, say, 10%, it can influence the price of a stock. What we're seeing with Shopify is consistent with that.

Expenses on the rise

Another factor that may have influenced Shopify's selloff is the company's rapidly growing expenses. Although Shopify is growing its revenue at about 58% a year, its costs are keeping pace: from 2014 to 2017, operating expenses grew from $126 million to $722 million. That's some serious cash Shopify is burning through.

This year, the company added about $500 million to it in the form of a swanky new Toronto office location. The goal of the Toronto office space investment is to attract programming talent to the company's new home in Canada's #1 tech city. But with a price tag that rounds to a billion dollars, it's still not clear that it will pay off.

Earnings: an uncertain future

Because Shopify's expenses are growing so fast, its earnings remain negative by GAAP standards. Although Shopify reported positive adjusted EPS of $0.04 in Q3, in non-adjusted terms the company had a net loss of $0.22 per share — a loss that was up from $0.09 per share a year before.

It's possible that these losses are simple growing pains for a company that, after all, only IPO'd in 2015. It's normal for tech stocks to run losses for years before becoming profitable. For example, **Amazon.com** went over a decade growing its business before it became consistently profitable, and it never stopped getting solid returns through all the years it was burning through cash.

In light of this, I'm not inclined to say that the negative earnings are a huge issue for Shopify (for now). In fact, the stock's 24% slide was most likely caused by the TSX crashing and amplified'by Shopify's higher-than-average volatility.

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Date
2025/08/26
Date Created
2018/11/28
Author
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