Is Shopify Inc. (TSX:SHOP) Stock Headed for Troubled Times?

Description

Shopify Inc. (TSX:SHOP)(NYSE:SHOP) stock has rallied for good reason.

Its leading cloud-based commerce platform designed for small and medium-sized businesses has filled a need that was screaming to be filled, with new and old business owners struggling to get a handle of the new online world of business.

This tech stock is transforming the e-commerce world.

But earnings estimates for Shopify have been falling, and this, coupled with its lofty valuations, makes it a bad place for investors to be.

The consensus EPS estimate for 2019 has been reduced to $0.40 from $0.59 previously, and while the consensus 2020 and 2021 estimate has held steady, this is a worrisome trend, as falling estimates are a precursor to weak stock prices.

And with Shopify's rich valuation, the stock is even more vulnerable to this dynamic.

Also, recent developments are causing concern, as the competitive environment looks to be getting more intense.

Although Shopify is still sitting comfortably in its leading competitive position, moves from the likes of Facebook's Instagram and from Mailchimp, a privately held firm out of Atlanta, aim to threaten its lead.

Facebook Inc.'s launch of Instagram Checkout, which allows consumers to pay for items without leaving the platform, aims to take Shopify out of the equation as it builds its own pop-up stores that accept payment as well as tests out a video platform that lets merchants sell products through real-time streaming videos.

This would be in direct competition with Shopify, and as the competitive landscape heats up, Shopify will certainly face headwinds as a result.

Next, let’s talk about developments out of Mailchimp, who once partnered with Shopify.

The company has now broken free from the partnership and has acquired a company named LemonStand, which is helping Mailchimp build out its e-commerce functionality.

Another threat to Shopify as another competitor aims to take part of Shopify’s pie.

As for Shopify stock, I actually see too much downside risk due to lofty valuations, which make the stock very vulnerable to any company-specific or industry developments and/or if the market takes a downturn, which it is looking increasingly likely.

With a yield curve that has now officially inverted in Canada, the bond market is telling us something that equity investors clearly do not want to hear.

And while an inverted yield curve does not guarantee a recession, it does increase the odds, and it does make prudent to adjust the risk level of our portfolios accordingly.

Bottom line

As we can see, the competitive environment is very fluid and at this time, it looks like it is heating up for Shopify.

And while there will certainly be room for more than one e-commerce platform, there is no question that investors need to closely follow these developments, especially given Shopify stock’s lofty valuation and high expectations priced into the stock as well as the precarious economic environment.

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