Hotter Than an IPO: Could Shopify Inc. (TSX:SHOP) Soar to $1,000 By Year's End?

Description

There's no doubt that **Shopify** (TSX:SHOP)(NYSE:SHOP) has been one of the hottest stocks in Canada this year. Shopify has been one of the most innovative companies to ever arise from the Canadian market, and there are a lot of things to adore about the company, most notably the cutting-edge innovation going on behind the scenes, the high growth ceiling, and the exceptional management team.

A business so wonderful rightfully deserves a premium price tag. But at what point does a premium become excessive?

If Shopify keeps up this momentum into the latter part of the year, we could see Shopify break the $1,000 mark. And although possible if the right cards fall into place (a continued rally in the broader tech market to go with more blowout quarters), I do think the odds of a drastic correction is far more likely given how high the bar has been set after the last quarter.

While Shopify is firing on all cylinders, there exists a price such that even the best business in the world becomes a sell. With shares of Shopify hovering at over $420 at the time of writing, I think Shopify is such an overheated stock that ought to be trimmed because of the risk of substantial downside.

After more than doubling since December lows, I wouldn't go as far as saying Shopify is in bubble territory, but valuations are stretched, and I do think the risk-reward trade-off is now highly unfavourable when you consider you're likely paying up for many years worth of growth right off the bat.

Simply put, the stock is priced for absolute perfection.

An IPO-like boom and bust coming for overbought Shopify stock?

At the time of writing, Shopify trades at over 28 times sales and 16.4 times book. These metrics make shares of Shopify comparable to a red-hot, oversubscribed IPO which have a magnitude of hype that drive the big booms and busts that come with “sexy” IPOs.

Although Shopify has proven itself in the public markets for many years, I do think the level of hype on the name today is to be feared, and that an IPO-like bust may be quick to follow the recent boom in the stock, especially should the broader rally in tech come to an end.

While I have no problem “paying up” for the stocks of hyper-growth companies, there comes a point where the valuations just fail to make sense anymore.

Yes, Shopify is doing a lot of things right,, but unless you’re comfortable with a 30-40% pullback from today’s levels, I’d recommend waiting patiently on the sidelines for an opportunity to bag Shopify on a dip, potentially below $280.

Foolish takeaway

If you’re in the stock, it can’t hurt to take a bit of profit off the table today. Heck, if you’re bullish on the name over the long term, then think about how many more shares you’ll be able to afford by buying on an inevitable dip.

Trimming a Shopify position undoubtedly comes with upside risk (risk of missing out on further upside), but I’d say the downside risk heavily outweighs any further upside at these levels. At this juncture, Shopify at $250 is looking much more likely than Shopify at $1,000.

The bar is set way too high, and no company can consistently knock it out of the ballpark every quarter, so wait for the inevitable quarterly miss and the pullback that’ll ensue.

Stay hungry. Stay Foolish.

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Date
2025/08/26
Date Created
2019/07/18
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