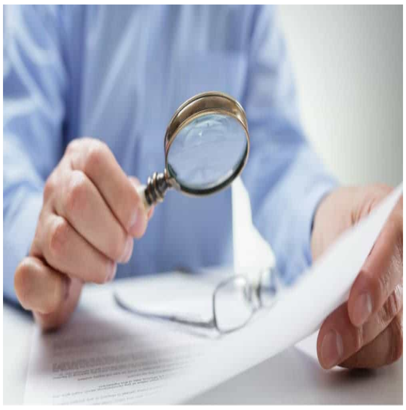

Why Shopify (TSX:SHOP) Stock Fell 19% in September

Description

Shares of Canada's e-commerce giant **Shopify** (TSX:SHOP)(NYSE:SHOP) lost close to 20% in September 2019. The stock is currently trading 178% below its 52-week high and 20% below its 52-week low.

Despite the recent pullback, Shopify is up by a stellar 138% year to date and has gained 1,055% since its IPO in May 2015.

Acquired 6 River Systems for $450 million

On September 9, Shopify announced the acquisition of 6 River Systems — a warehouse robotics and software company. Shopify stated that around 40% of the acquisition will be financed by issuing new stock.

On September 17, Shopify raised $600 million in a secondary offering at a price of $317.5 per share. This offer price was considerably below the stock's trading price of $338 on September 16, which drove shares lower.

We know that Shopify will be raising $1 billion over the next five years to set up its own fulfillment centres. According to Shopify. once these centres are up and running, it will be able to store and package shipments on behalf of channel partners.

This secondary offering will be used to set up Shopify's fulfillment centres and finance the acquisition of 6 River Systems.

Does Shopify management think shares are overvalued?

We have seen how Shopify has considerably grown investor wealth over the years. But does the management think that the stock is overvalued, or did they price the secondary offering lower to easily raise capital? The public filings show that company insiders have sold close to 270,000 shares worth $43 million over the last 12 months.

Insider selling is not viewed as a positive by investors, and this too would have dragged Shopify shares lower over the past month.

What next for investors?

Now that Shopify is trading 20% below its 52-week low, is it a good time to buy the stock? Not quite. Investors are still worried about sky-high valuations in the technology sector. The last month saw a tech sell-off that was led by overvalued stocks including Shopify, **BlackBerry**, **Cloudera**, **LightSpeed**, and many others.

Yes, Shopify shares have gained 5% in market value this month but are still vulnerable in an uncertain microenvironment. The stock is still trading at a premium valuation. Growth stocks have a high beta, which means though they are a solid bet in a bull run, investors will burn significant wealth in a bear market. Shopify stock has a three-year beta of 1.24.

Though Shopify generates in excess of $1 billion in yearly sales, it is still struggling to be profitable on a GAAP basis. Analysts, in fact, estimate Shopify’s net margin to fall from -6% in 2018 to -7.1% in 2019. Shopify is estimated to post a net loss until the end of 2021.

Now, with the investments in setting up fulfillment centres, there is a good chance that profit margins will move lower. Analysts expect Shopify to increase earnings by 60.5% in 2019 and 55.7% in 2020. These estimates might have to be revisited due to the recent acquisition and increasing capital-expenditure investments as stated.

Shopify stock is trading at a forward price-to-earnings multiple of 344. This is really expensive looking at the company’s five-year estimated annual earnings growth of 53%. The broader markets remain volatile and are bound to move lower as we head into the last quarter of 2019. This will negatively impact Shopify and other growth stocks as well.

Analysts remain optimistic about Shopify and have a 12-month average target price, which is 10.6% higher than the current trading price.

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