Shopify (TSX:SHOP) Is Canada’s Most Valuable Company: Is It Justified?

Description

As of market close on Friday, **Shopify Inc** (TSX:SHOP)(NYSE:SHOP) was the most valuable company in Canada, with a $163 *billion* market cap. That’s more than $30 billion more than the second most valuable company, the **Royal Bank of Canada**. While Canadian markets were closed on Monday, Shopify scored another winning day in the U.S. markets on that date. By the time you read this, SHOP’s market cap in Canadian dollars will likely be even higher than it was on Friday.

For long-time Shopify shareholders, this is all good news. If you’d bought SHOP at its IPO price and held to today, you’d be up about 4,000% by now. That’s a massive gain. But it all raises the question of whether this can go on for much longer.

If Shopify kept up its recent gains for three more years, it would be a trillion dollar company. That’s for a company that only earned $36 million–in GAAP terms–in the second quarter. It would take an extremely long time for Shopify’s earnings to catch up with its stock price, even with all the growth we’ve been seeing. As you’re about to see, though, that doesn’t necessarily make the stock overvalued.

A steep valuation

By conventional metrics, SHOP is an extremely expensive stock. It trades at over 60 times sales and has a 550 forward P/E ratio based on **Thomson Reuters’** earnings projections. Before the company’s strong Q2 results, the estimated P/E ratio was 1,400. For the trailing 12-month period, the company’s GAAP earnings remain negative. Adjusted earnings have been positive for about a year.

That doesn’t necessarily make it overvalued

While SHOP's valuation is very steep, the stock isn't necessarily too expensive. The reason is that the company is seeing incredible growth. in Q2, SHOP grew its revenue by 97% year-over-year. In previous quarters, the growth rate had been closer to 47%. So now, Shopify's growth is not onlystrong, but also accelerating.

To an extent, this is in keeping with what was predicted. Everybody knew that the closure of retail businesses in the COVID-19 era would lead to more e-commerce purchases. SHOP's Q2 earnings were a natural consequence of that. The question is whether this growth can be maintained after life goes back to normal.

That's not an easy question to answer. While businesses are increasingly *permitted* to re-open, many retailers are closing permanently. So it's possible that the e-commerce industry will lock in its sales boost long-term.

Foolish takeaway

For years, Shopify has been one of Canada's best-performing stocks. Today, it still holds that distinction, while also carrying the title of the nation's most valuable company. As we saw in Q2, SHOP is generating the kinds of results that justify a premium share price.

The question is whether they truly justify the steep prices we're seeing today. That question is too broad for the scope of this article.

I will say that if you want some SHOP exposure in a less risky package, you could consider a large cap **TSX** ETF like the **iShares S&P/TSX 60 Index Fund**–Shopify is its largest single holding, worth about 8% of NAV and rising.

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Date
2025/08/25
Date Created
2020/08/04
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