



## Should Shopify (TSX:SHOP) Really Be Worth More Than Royal Bank of Canada?

### Description

Shares of **Shopify** ([TSX:SHOP](#))([NYSE:SHOP](#)) have continued to defy the laws of gravity in 2020. With profound pandemic tailwinds still at the e-commerce kingpin's back, investors wonder if the stock has any more multiple expansion left in it. The firm has made a habit out of posting blowout quarter after blowout quarter. And while the firm may still be in the early innings of its long-term growth story, investors need to be cautious overpaying up for many years' worth of growth right off the bat.

### The stock market looks pretty darn expensive these days!

However, in a [prior piece](#), I noted that the premium price tag on your average stock was completely warranted, given the unprecedented type of market environment we currently find ourselves in. The U.S. Fed's willingness to do anything to help the economy recover from the COVID-19 crisis is seen as a green light for many to neglect traditional valuation metrics that have expanded greatly in recent months.

In the case of Shopify, the stock continues to look unstoppable, with shares trading near the 60x sales mark (that's sales, not earnings!). Clearly, investors are pounding the table on Shopify's growth story and are more than willing to run the risk of overpaying for many years' worth of growth upfront.

There's no question that white-hot growth stocks like Shopify deserve a lofty valuation. But just how much a premium remains the million-dollar question.

With more than just perfection baked into the stock, I'd urge investors only to invest what they're willing to lose on a name that trades a nosebleed-level valuation that's above and beyond that of "frothy" Silicon Valley darlings that look like bargains in comparison. Simply put, Shopify stock at these heights is a risky proposition that could lead to amplified losses if growth stocks are to take a backseat to value plays in the new year.

Given the odds of a growth-to-value or growth-to-reopening rotation in the new year, I'd say that investors should expect more turbulence from the name and should seek to scale into a full position over time.

## Shopify looks to expand its lead on Royal Bank

With Shopify's \$176 billion market cap, the white-hot tech sensation has left **Royal Bank of Canada** ([TSX:RY](#))([NYSE:RY](#)) and its \$149 billion market cap behind in the dust.

Fool contributor Chris MacDonald [recently noted](#) that Royal Bank had more earnings than Shopify had revenues despite being worth less. MacDonald also warned that those paying up to invest in Shopify's "story" were at risk of being left holding the bag if it turns out that tech stocks are partying like it's the late 1990s.

"Many of the mega-cap technology companies traded in the U.S. have seen valuations balloon to levels not seen in some time. The dot-com bubble is often cited as the most recent example of when we saw such valuations on the NASDAQ." wrote MacDonald.

"Some investors say high valuations are here to stay, particularly if interest rates stay low for a very long time. That being said, over the very long term, valuations tend to revert toward the longer-term mean. Momentum investors could be in for a rude awakening if we do see such a scenario take place."

Some investors who think Shopify ought to be worth more than an old-school bank, are going all-in on the story. And to the skeptics, Shopify may rhyme with past bubbles that had their day at the top of the **TSX**. Only time will tell if Shopify can retain or expand upon its lead on Royal Bank.

Indeed, there are risks on both ends: downside and upside risks.

## Foolish takeaway

If it turns out that lofty tech valuations are not in need of a fast-and-furious correction, those shunning such plays could be left on the sidelines as they watch epic rallies continue. That's why I'm a huge fan of playing both sides of the equation by nibbling Shopify and other tech stock on dips while also having a foundation with names like Royal Bank, whose valuation is backed by robust, high-quality earnings.

I think investors would be wise to heed MacDonald's words of warning by not ignoring valuation, even though doing so may have led to superior returns in 2020.

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### TICKERS GLOBAL

1. NYSE:RY (Royal Bank of Canada)
2. NYSE:SHOP (Shopify Inc.)
3. TSX:RY (Royal Bank of Canada)
4. TSX:SHOP (Shopify Inc.)

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## **Date**

2025/09/15

## **Date Created**

2021/01/05

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