Shopify (TSX:SHOP) Stock's Growth Will Slow

Description

Shopify (TSX:SHOP)(NYSE:SHOP) has been one of the best-performing stocks of the past decade. Since its IPO in 2015, it has risen 4,000%. Not many stocks can boast growth that rapid. And it looks like Shopify itself isn't expecting it going forward. In its recent earnings release, the company told investors to expect deceleration. Indeed, its most recent quarter did show a slower growth rate than the quarter before (sequentially). In this article, I'll explore the likely revenue deceleration coming, and what it means for Shopify's stock.

What is deceleration?

Revenue growth deceleration is when a company's revenue is growing but the *rate* of growth is slowing down.

Let's say a company had the following revenue figures for 2018, 2019, and 2020:

- 2018: $100
- 2019: $200
- 2020: $250

The years 2019 and 2020 both saw revenue increase over the prior year. But the rate of growth slowed. The 2019 rate was 100%; the 2020 rate was only 25%. When this happens, a company may still technically be in the growth stage. But it's likely to fall short of the growth rates investors expected and on which its stock was valued. If deceleration is extreme enough, it may cause a company's stock to decline in price.

So, why is this such a concern for Shopify?

First of all, it has happened before. Went it went public, Shopify grew revenue at 90% over the prior year. In the years that followed, the growth rate whittled all the way down to 45%. 45% is still strong,but if investors expect you to double your revenue, it's a miss.

Now, eventually, Shopify did get its revenue growth rate back above 90%. Specifically, it grew at 96% and 97% in the second and third quarters of 2020. However, that was largely due to COVID-19. The COVID-19 pandemic forced many retail stores to shut down. As a result, consumers flocked to online stores, which Shopify provides the infrastructure for.

Eventually, the COVID-19 pandemic will end. It may not be this year, or even next year, but it will happen eventually. When it does, the main catalyst powering Shopify's superior growth will be gone. The company is aware of this, so now it's warning investors to expect slower growth going forward.

The stock itself probably won't see as much appreciation

What all this adds up to is the fact that SHOP likely won't produce the kinds of returns in the future that it did in the past.

SHOP has had an incredible run. In its six years as a public company, it has doubled in value every year but one. At its current growth rate, it would be a trillion-dollar company in just three years!

That's a tantalizing scenario to imagine. But it's unlikely to actually play out. SHOP may join the trillion-dollar market cap club eventually, but with revenue growth deceleration looming, it's going to take longer than three years. That doesn't mean that the stock isn't worth owning. On the contrary, its recent dip makes for an interesting entry point. But it does mean that investors will need to temper their expectations. No stock doubles in value every year for all eternity.

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