Why Shopify (TSX:SHOP) Soared 9% After Earnings

Description

Last week, investors got a rare treat after **Shopify** (TSX:SHOP)(NYSE:SHOP) missed badly on earnings but rallied anyway. SHOP was at $1,663 when it reported before market open on Thursday. By the close on Friday, it was at $1,807–an 8.66% gain. This huge gain was made all the more remarkable by just how badly Shopify missed. Analysts were expecting $1.42, SHOP actually delivered a mere $0.81. Earnings were a full 42.9% lower than what analysts expected. Clearly, there was something going on in these earnings that investors liked. The question is, what was it?

GAAP earnings better than adjusted

An important thing to note about Shopify's earnings miss is that it was a miss on *adjusted* earnings.

The GAAP earnings were actually massive, coming in at $9 per share.

When you look at EPS estimates for any given stock online, they're all just lumped together into a single number. But in fact, analysts may be talking about different things when they say EPS. GAAP EPS goes by the accounting rules. Adjusted EPS goes by whatever management believes is most accurate. Shopify's miss was on adjusted earnings. By conventional accounting standards, it actually did very well.

Why report two different sets of earnings?

Sometimes management doesn't think that GAAP accounting rules produce a number that reflects how they actually did. In Shopify's case, the $9 in GAAP earnings was mostly due to stock market gains. Shopify didn't sell the shares that it made these big gains on, so the gains didn't affect its operating performance. For this reason, it chose to exclude the unrealized gains, which have to be included according to GAAP, from adjusted EPS.

Basically, if you include Shopify's gains on its stock portfolio, it did much better than what was reported in the media. Asset managers may have taken note of that and bought the stock accordingly.

Other tech stocks disappoint

Another factor that may have helped Shopify is the fact that many other tech stocks disappointed last week. In the same period when Shopify reported its biggest GAAP EPS ever, **Apple** missed badly on revenue, and **Amazon** missed on both revenue *and* earnings. Shopify only just barely missed on revenue, while the other two companies mentioned missed by a mile. So, while Shopify's adjusted EPS was a dud, it at least had about the level of sales growth that was expected. This may have made it look better than other tech stocks, which largely disappointed in Q3 — especially compared to Q2's blockbuster results.

Foolish takeaway

Big tech earnings season is just about over, and it's looking like it was a disappointment. Sure, there were some bright spots, but many of the biggest tech companies fell short of expectations. Shopify was one of those that missed, sure, but there were some bright spots in its quarterly report that may have contributed to its massive 9% rally.

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