



Keep These 3 Characteristics in Mind When Choosing Growth Stocks

Description

[Growth stocks](#) have been losing massive amounts of value since the start of the year. This has split investors into two camps. The first group would rather not buy any growth stocks. Instead, they would rather put money into safer options like dividend stocks. The second group, and the one I identify with, see this as an excellent opportunity to buy shares of excellent companies at a massive discount.

However, growth investing is difficult. In many cases, investors don't have a lot of data to work with when assessing companies. This is especially true with recent IPOs. However, it's possible to make growth investing a bit easier. Investors should develop a set of filters that they use to screen every prospective company. In this article, I'll provide examples of three characteristics I look for in growth stocks that I consider adding to my portfolio.

The stock must lead an important and emerging industry

This characteristic is self-explanatory. I believe that the best growth stocks are those that lead important *and* emerging industries. This is a characteristic that I've taken from David Gardner's Rule Breaker investing method. However, it makes perfect sense.

There are many clear examples of this in the American stock market. For example, **Apple** took charge in the mobile phone industry in the early 2010s. Since then, the company has expanded its first-mover advantage in that industry and expanded into more areas of consumer tech. Little explanation needs to be said about how much Apple stock has grown since. Over the past five years alone, Apple stock has gained 369%!

In Canada, **Shopify** ([TSX:SHOP](#))([NYSE:SHOP](#)) is a good example of a company that leads an important and emerging industry. In fact, it has grown into being one of the largest players in the global e-commerce industry. The company provides a platform that businesses can use to operate online stores. What makes Shopify so intriguing is that its solutions appeal to both first-time entrepreneurs and large-cap enterprises. As e-commerce continues to grow, it becomes even harder to imagine a future where Shopify isn't a household name.

There must be evidence of strong growth

Next, investors should look for evidence of strong growth. This can be interpreted in many ways, with revenue being the easiest way to measure growth. Personally, I check to see whether a company has managed to continue increasing its revenue in each of the past five years. If a company passes that initial check, then I consider it more strongly as a potential stock to add to my portfolio.

In Shopify's most [recent earnings presentation](#), we can see that the company has reported an increasing monthly recurring revenue in every quarter since Q4 2016. Since that quarter, Shopify's MRR has grown at a CAGR of 41%. This growth is supported by a consistent increase in Shopify's gross merchandise volume. In 2017, the company reported a GMV of US\$26.3 billion. In 2021, Shopify's GMV totaled US\$175.4 billion. This suggests that its platform is continuing to grow, as it sees a lot more transactions each year.

Looking at the company's management

Finally, investors should look at a company's management team. The first aspect of a company that I look at is whether it's founder led. Research has shown that stocks of founder-led companies tend to outperform those led by non-founders. In addition, I would like to see the company's CEO hold at least a 5% ownership in the company. If a company satisfies this requirement, then it tells investors that the CEO is willing to be rewarded according to the company's success. It also aligns the CEO's interests with shareholder interest.

Shopify satisfies both requirements. Its founder Tobi Lütke was actually responsible for writing the very first line of code in what would eventually become Shopify's platform. In addition, he holds a 6.27% ownership stake in the company.

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Date

2025/07/03

Date Created

2022/03/17

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