TSX Tech Stocks Continue to Drop: What Should Investors Do?

Description

This is indeed a tough time for growth investors. TSX tech stocks are down almost 35% this year, while the **TSX Composite Index** is just marginally down. Notably, the macro situation is getting uglier for tech stocks, with Treasury yields at multi-year highs and the severely hawkish stance of the Fed. As a result, even seasoned contrarian investors feel puzzled about the continual weakness in tech stocks this year.

Why TSX tech stocks are falling

When interest rates increase, the discount rate to value stocks increases, ultimately making the present value of their future cash flows lower. That's why the stock's intrinsic value declines in the rising-rate environment, and we see lower price targets from analysts.

Canadian tech giant stock **Shopify** (TSX:SHOP)(NYSE:SHOP) has lost almost two-thirds of its value in the last six months. The stock has fallen from $2,229 levels in September to $585 last week.

In the case of SHOP, a confluence of damaging factors weighed on the stock. First, there was a low-growth outlook the company guided amid the end of the pandemic. Moreover, faster-than-expected interest rate hike prospects brought down Canada's one of the most richly valued stocks.

It will be interesting to see whether its Q1 2022 earnings bring some respite to SHOP stock and its investors. The management has already cautioned investors that upcoming numbers will be muted. However, some operational growth and a relatively upbeat commentary might help the stock to some extent.

On the valuation front, SHOP stock is now trading 25 times its earnings, and I think it is reasonably valued. However, that does not mean there will be a one-way recovery. Rising Treasury yields and rapidly increasing inflation, mainly amid the Russia-Ukraine war, could make things worse. But I think SHOP's lower growth outlook and the Fed's faster rate hikes seem to have already priced in the stock.

What’s next for NVEI stock?

The second one that saw a massive fall is **Nuvei** (TSX:NVEI)(NASDAQ:NVEI). After topping the top-gainer charts for most of last year, NVEI has been one of the laggards in 2022. The payment processor stock is currently trading at $74, down from its record $180 in September last year.

Nuvei’s fall has been due to a combination of its sky-high valuation and a short report. However, the company has maintained its growth outlook for the long term. It expects 30-35% revenue growth with +50% EBITDA margins for the foreseeable future.

Despite handsome growth potential, NVEI stock is trading at 80 times its earnings and 15 times sales. So, some negative catalysts like lower-than-expected quarterly performance and faster rate hikes could see an outsized impact on the stock.

Nuvei caters to the large addressable market and indeed offers fine-looking growth prospects. However, conservative investors should avoid buying growth at any price.

Another victim of the current tech selloff and a short report was **Lightspeed Commerce** (TSX:LSPD)(NYSE:LSPD). Its peculiar to see tech stocks riding high this time last year. But as the pandemic fears waned and policy tightening gained steam, growth stocks like LSPD changed their course. Notably, the stock has fallen 83% since September 2021.

Loss-making companies with stretched valuations tumble big in a rising-rate environment. The same thing happened with LSPD. A company with barely US$484 million in revenues boasts a market cap of $4.2 billion.

Bottom line

Among the three, I think SHOP offers an attractive risk/reward proposition at the moment. One could start accumulating Shopify shares at these levels and keep cash to buy the dip.

CATEGORY

1. Investing
2. Tech Stocks

TICKERS GLOBAL

1. NASDAQ:NVEI (Nuvei Corporation)
2. NYSE:LSPD (Lightspeed Commerce)
3. NYSE:SHOP (Shopify Inc.)
4. TSX:LSPD (Lightspeed Commerce)
5. TSX:NVEI (Nuvei Corporation)
6. TSX:SHOP (Shopify Inc.)

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