Down 80% From Record Highs, Is Shopify Stock Undervalued Right Now?

Description

Shopify (TSX:SHOP)(NYSE:SHOP) is one of the largest e-commerce companies in Canada. It is also among the fastest-growing companies based in the country and is rapidly expanding its market reach to other regions. However, the stock has been hard hit by the ongoing tech rout and is currently down 72.18% year to date. Moreover, SHOP is currently trading nearly 80% lower than its 52-week high of $2,228.73.

Shopify stock split and valuation

Taking cues from tech giants such as **Amazon**, **Tesla**, and **Microsoft**, Shopify announced a stock split in April. While a stock split is viewed as a positive development, the ongoing selloff surrounding growth stocks had dragged Shopify stock significantly lower in recent months.

Despite the downward spiral, SHOP shares are currently trading at sky-high valuations. It is currently trading at 388.30 times its forward non-GAAP earnings, which is significantly higher than the peer average of 17.68. Also, SHOP's trailing-12-month price-to-cash flow multiple stands at 149.36 compared to a peer average of 16.39.

However, the stock is trading 8.09 times its forward sales, which is quite reasonable.

Earnings outlook for Shopify

Shopify's loss margins widened significantly in the fiscal first quarter amid substantial macroeconomic headwinds and supply chain disruptions. It reported the slowest revenue growth in company history, disappointing investors.

Moreover, Shopify reported a loss of US$1.47 billion in the fiscal first quarter compared to a net income of $1.26 billion income in the year-ago quarter. Its operating cash outflow amounted to US$53.56 million in Q1 compared to a US$135.68 million inflow in the same period last year.

This trend will likely continue, as economies worldwide hike their interest rates to counter the inflationary challenges. Moreover, as the global supply chain bottlenecks persist, SHOP's earnings outlook seems bleak. The company's EPS is expected to decline 88% in the fiscal second quarter and 85.3% in fiscal 2022.

A look at its Deliverr acquisition

Earlier in May, Shopify's board of directors approved the acquisition of fulfillment technology partner Deliverr, Inc. for US$2.1 billion, marking its expansion to the logistics industry.

Regarding this, Tobi Lütke, Shopify's CEO, said, "Our goal is to not only level the playing field for independent businesses, but tilt it in their favour — turning their size and agility into a superpower … Together with Deliverr, Shopify Fulfillment Network will give millions of growing businesses access to a simple, powerful logistics platform that will allow them to make their customers happy over and over again."

However, the acquisition is expected to hurt SHOP's profit margins and return on equity in the near term. The company expects its operating margins to decline in fiscal 2022 primarily due to this merger, while capex is expected to increase substantially as well.

The Foolish takeaway

Growth stocks like SHOP tend to be the worst affected in a hawkish environment. As interest rates rise, borrowing costs for rapidly expanding companies increase drastically, shrinking their profit margins.

Also, the recent tech selloff has caused SHOP shares to lose more than 80% of their value since their November 2021 highs, making the tech heavyweight one of the worst-performing Canadian stocks in 2022. But it also offers investors an opportunity to buy a quality growth stock at a lower multiple.

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araghunath