Will Shopify's Stock Price Soar in 2023?

Description

Shopify (TSX:SHOP) was the most valuable company in Canada in 2021. Since then, the stock has nose dived 77%. Canada's most popular tech stock is now the poster child of the great pandemic bubble.

Investors like me now wonder if the correction is over or if there's more pain ahead. Here's a closer look.

Key drivers

The macroeconomy is the key driver of Shopify stock this year. We already know Shopify has excellent management and a robust ecosystem of tools that merchants rely on. However, none of this matters if consumer sentiment and e-commerce penetration is slowing down.

That's what happened in 2022. Inflation reared its ugly head and central bankers across the world raised interest rates sharply to deal with it. The U.S. Fed funds rate jumped from 0.25% to 4.5% last year. Meanwhile, the Bank of Canada raised borrowing costs from 0.25% in March 2022 to 4.25% in December 2022.

Higher interest rates impact growth stocks like Shopify because they make their valuations less attractive and their customers less wealthy. Shopify's stock valuation has plunged from 60 times revenue to just 8.4.

What lies ahead?

There are reasons to be optimistic about Shopify. For one, revenue growth is still robust. The company had a record-breaking Black Friday and Cyber Monday season. Sales were up 19% from the previous year. Christmas shopping data should be out soon.

Meanwhile, Shopify raised capital during the pandemic. It now has US$4.9 billion, or CA$6.7 billion, in cash on its books. That’s nearly 11% of its market value. The company also cut staff to reduce costs and launched new products to help large retailers integrate the platform, raise capital, or advertise on its network. These efforts should boost growth.

The macroeconomic picture is changing, too. Inflation is well past its peak. The official inflation rate cooled from 8.13% to 6.8% in the last six months. Analysts believe this trend could continue and the Bank of Canada expects inflation to slide to 3% by the end of 2023 and 2% by the end of 2024.

Hitting this target should ease the pressure on interest rates. The Bank of Canada doesn’t need to keep rates elevated by next year, which means growth stocks should see a rebound in valuations. Shopify may never hit 60 times revenue, but even modest growth (20%) and a reasonable valuation (10 times revenue) could deliver robust gains in the year ahead.

Bottom line

Shopify has become the poster child of the pandemic boom. Its growth and valuation were stretched to the stratosphere. Now, the pendulum has swung and the stock is down 77% from its peak. It’s now much more attractive for long-term growth investors willing to take a contrarian approach.

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