

Shopify Inc. (SHOP)

\$377.78 (As of 03/12/20)

Price Target (6-12 Months): **\$321.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 02/23/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:C

Value: F

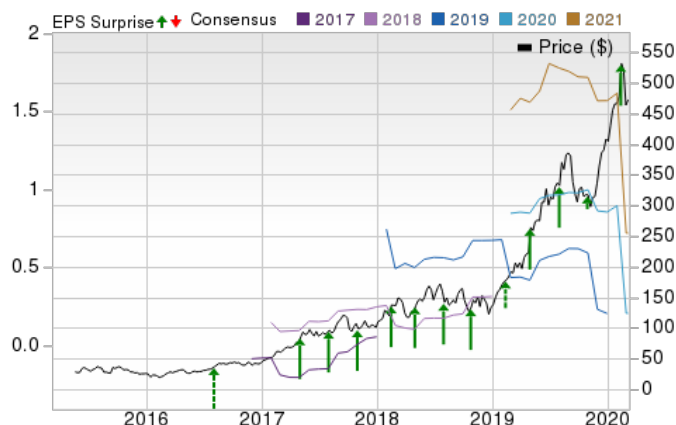
Growth: A

Momentum: C

Summary

Shopify's increasing spend on fulfillment network, infrastructure and platform is likely to impede margin expansion in the days ahead. In a bid to maintain competitive position in the e-commerce market, Shopify is increasing investments on product development, which is likely to weigh on the company's financial performance at least in the near term. Stiff competition from Amazon, eBay, Square, Facebook's Instagram Checkout, among others, is a concern. It can be noted that, management intends to invest \$1 billion over the subsequent five years to develop the new fulfillment network. Moreover, lack of big-shot international customers is a headwind for Shopify. Additionally, the company focuses on the SMB segment which is more susceptible to macro-economic headwinds and makes the business challenging.

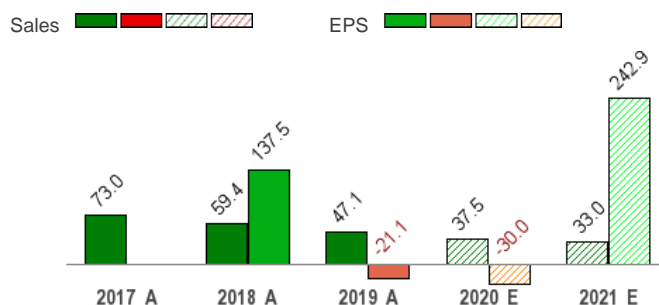
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$593.89 - \$190.38
20 Day Average Volume (sh)	2,741,512
Market Cap	\$43.6 B
YTD Price Change	-5.0%
Beta	1.13
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Internet - Services
Zacks Industry Rank	Top 36% (91 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	87.0%
Last Sales Surprise	4.8%
EPS F1 Est- 4 week change	-113.6%
Expected Report Date	05/05/2020
Earnings ESP	-8.2%
P/E TTM	478.2
P/E F1	1,799.0
PEG F1	49.3
P/S TTM	27.6

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	603 E	666 E	707 E	903 E	2,887 E
2020	446 E	498 E	535 E	684 E	2,170 E
2019	320 A	362 A	391 A	505 A	1,578 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	-\$0.01 E	\$0.08 E	\$0.15 E	\$0.46 E	\$0.72 E
2020	-\$0.17 E	\$-0.00 E	\$0.09 E	\$0.33 E	\$0.21 E
2019	\$0.09 A	\$0.14 A	\$0.13 A	\$0.43 A	\$0.30 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 03/12/2020. The reports text is as of 03/13/2020.

Overview

Ottawa, Canada-based Shopify Inc. (SHOP) provides a multi-tenant, cloud-based, multi-channel commerce platform for small and medium-sized businesses (SMBs). The company completed Initial Public Offering (IPO) in May 2015.

Merchants use the company's software to run business across various sales channels, including web and mobile storefronts, physical retail locations, social media storefronts, and marketplaces.

Shopify's platform enables merchants to manage products and inventory, process orders and payments, ship orders, build customer relationships and leverage analytics along with reporting from one integrated back office.

Moreover, Shopify hosts a huge database of merchant and customer interactions. Merchants leverage this transactional dataset to get meaningful insight into the sales channel growth prospects and consumer behavioral aspects. This improves their ability to target prospective customers more easily, which drives sales growth.

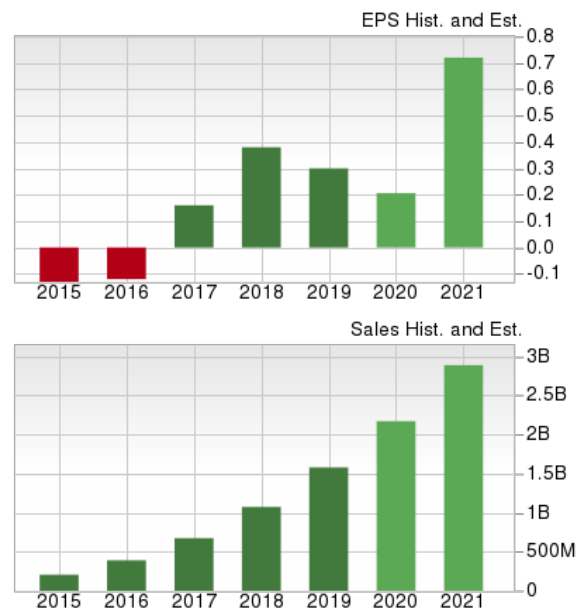
Apart from the company's own payment solution, payment wallets like Apple Pay, Google Pay is also available to the merchants, which they offer to customers for completing transaction done on the Shopify platform.

In 2019, revenues came in at \$1.578 billion. The company generates revenues from two sources: Subscriptions Solutions (40.7% of 2019 revenues) and Merchant Solutions (59.3%).

Subscription revenue is recognized on a ratable basis over the contractual term. The terms range from monthly, annual or multi-year subscription terms. The company earns revenue based on the services it delivers either directly to merchants or indirectly through resellers.

Shopify generates the majority of merchant solutions revenue from fees that it charges merchants on their customer orders processed through Shopify Payments.

The company also derives merchant solutions revenue relating to Shopify Shipping, Shopify Capital, other transaction services and referral fees, as well as from the sale of Point-of-Sale (POS) hardware.



Reasons To Sell:

- ▼ Shopify is relatively a new player in the eCommerce marketplace. Although it is not a direct competitor to behemoths like Alibaba and Amazon, many of its customers are. This presents significant risk for its growth prospects.
- ▼ Moreover, the company focuses on the SMB segment which is more susceptible to macro-economic headwinds and makes the business challenging.
- ▼ Furthermore, lack of big-shot international customers is a headwind for Shopify. The company doesn't have significant presence in the Asia-Pacific market, which is fastest growing retail eCommerce market according to eMarketer. This is a major deterrent in our view.
- ▼ We believe that increasing investments on product development, Shopify Plus and cloud infrastructure will make it difficult for the company to sustain profitability. Moreover, it expects to further increase research & development (R&D) expense. Markedly, management intends to invest \$1 billion over the subsequent five years to develop the new fulfillment network, which is likely to impact margin expansion. We also note that Shopify has been incurring losses in the last three years and has an accumulated deficit of \$304.2 million as of Dec 31, 2019. Despite the improving top line, mounting losses doesn't bode well for investor confidence.
- ▼ The company is trading at premium in terms of Price/Book (P/B). Shopify currently has a trailing 12-month P/B ratio of 14.45X, which compares unfavorably with what the industry witnessed over the last year. Hence, valuation looks slightly stretched from P/B perspective.

Shopify's focus on SMB segment, lack of international exposure, increasing operation expenses and stretched valuation are primary negatives.

Risks

- Market research firm eMarketer estimates global retail eCommerce sales (excluding travel, restaurant and event ticket sales) to grow to \$893.4 trillion by 2022, which will make up 14.8% of total retail spending. We believe that the massive growth in eCommerce spending bodes well for Shopify. The company's cloud-based platform is well-positioned to address the growing needs of merchants at a time when social media, mobile devices and data analytics are transforming the eCommerce market place.
 - Shopify's biggest USP lies in the fact that it is a brand oriented platform as compared with an online marketplace. Here, the brand hogs the limelight, which helps the merchant win customer much faster through focused interaction. The platform helps in improving customer's brand loyalty, which drives merchant revenues. Further, we note that Shopify hosts a huge database of merchant and customer interactions. Merchants leverage this transactional dataset to get meaningful insight into the sales channel growth prospects and consumer behavioral aspects. This improves their ability to target prospective customers more easily, which drives sales growth. Management noted that merchants on average became more successful on Shopify, as number of merchants with GMV exceeding \$1 million grew 44% in 2019. Notably, in 2019, GMV of \$61.1 billion surged 49% over 2018. The company's plan to invest on leveraging this transactional data will further enhance merchant's ability to attract customers going ahead. We believe that the company's merchant focus strategy will aid it to dominate the SMB eCommerce market in the long run.
 - Moreover, the company continues to add functionality to its platform, which is responsible for driving merchant base. The launch of Shopify Payments, Shipping and Capital have made it easier for merchants to process payments, ship products and secure financing for their working capital needs, respectively. Notably, the percentage of merchants using Shopify Payments grew every quarter throughout 2019. The company has introduced Shopify Payments across 15 countries to date. Moreover, merchant adoption of Shopify Shipping continues to expand in both the U.S. and Canada. Management anticipates this trend to continue as the company expands shipping partners and add new features. Shopify is also working on extending language capabilities beyond English. In fact, Shopify reported merchant base of 29% from outside of core geography (with significant non-English-speaking population) in 2019, comparing favorably with 24% in 2018. Further, the company recently rolled out Shopify Fulfillment Network in the United States, for the first time, to facilitate commerce. We believe that its merchant focus business model will help it to achieve its growth target in the long haul.
 - Shopify is expected to add new merchants on its platform on the back of new sales channels like Google Pay, Facebook Messenger, Instagram, Pinterest, eBay and Amazon. Shopify noted that the addition of Houzz, Wanelo, eBates and others has driven the number of channels over which a merchant can sell to more than a dozen. The company also noted that merchants are buying more apps through app store, which is positive. Shopify app store currently offers around 3,700 apps. Moreover, availability of Apple Pay and addition of Canada Post are some other notable developments that will boost merchant base. We also believe that the company's strong partner referral system will boost merchant base that will eventually drive top-line growth in 2020. More than 24,500 partners referred merchants to Shopify in the past 12 months.
 - Mobile focus provides significant leverage to Shopify. The company launched its iPhone-based Shopify Mobile application way back in 2010. Also, the company released Shopify Ping for Apple's iOS devices, which is compatible with Facebook and Instagram ads and is enabled for Apple Business Chat. Mobile traffic to merchants' stores continued to grow, reaching 80% of traffic and garnered 68% of orders for the quarter ended Dec 31, 2019, up from 78% and 66%, respectively, reported in the year-ago quarter. We note that Shopify is benefiting from retail's rapid transition to mobile and social sales channels. In fact, Shopify platform garnered GMV of approximately \$2.9 billion in the Black Friday-Cyber Monday period in 2019. Notably, year-ago GMV figure in the same period stood at \$1.8 billion. Management noted that around two thirds of online orders from the U.S.-based Shopify merchants were registered via mobile devices.
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Last Earnings Report

Shopify Q4 Earnings Surpass Estimates

Shopify Inc. reported fourth-quarter 2019 adjusted earnings of 43 cents per share, surpassing the Zacks Consensus Estimate by almost 87%. Moreover, the figure improved 59.3% on a year-over-year basis.

Total revenues surged 47% from the year-ago quarter to \$505.2 million, outpacing the Zacks Consensus Estimate of \$482 million. The figure also fared better than management's guided range of \$472-\$482 million.

The top line benefited from an improving merchant base, rapid expansion in international markets and strong holiday sales in Black Friday/Cyber Monday period. The company continues to launch a number of merchant-friendly applications to meet the requirements of a dynamic retail environment, in turn strengthening merchant base.

Quarter in Detail

Subscription Solutions revenues (36.3% of total revenues) surged 37% to \$183.2 million driven by persistent growth in Monthly Recurring Revenue (MRR) due to the addition of several new merchants.

As of Dec 31, 2019, MRR was \$53.9 million, up 32% from the year-ago quarter. Shopify Plus accounted for \$14.6 million, representing 27% of MRR compared with 25% in the quarter ended Dec 31, 2018.

Merchant Solutions revenues (63.7%) advanced 53% to \$322 million, primarily on account of growth in Gross Merchandise Volume (GMV), which improved 47% from the year-ago quarter to \$20.6 billion.

Shopify Capital advanced \$115.9 million cash to merchants in the reported quarter, surging 61% compared with \$71.8 million in the year-ago quarter. Notably, since the launch of Shopify Capital, cumulative merchant cash advances have improved to \$885 million, out of which \$150 million was outstanding as of Dec 31, 2019.

Shopify Shipping witnessed robust adoption in the fourth quarter. The offering is being leveraged by 45% of total eligible merchants across the United States and Canada.

Gross Payments Volume (GPV) came in at \$8.9 billion, accounting for 43% of GMV processed in the fourth quarter, up from \$5.8 billion (41%) in the prior-year quarter.

Purchases from merchants' stores especially from mobile devices witnessed 80% of traffic and garnered 68% of orders for the quarter ended Dec 31, 2019, up from 78% and 66% reported in the year-ago quarter, respectively.

Operating Details

Non-GAAP gross profit (adjusted for amortization of acquired intangibles) surged 43.7% year over year to \$269.9 million. This can be attributed to robust performance of Shopify Plus and Shopify Capital.

Non-GAAP gross margin contracted 200 basis points (bps) from the year-ago quarter to 53%.

Shopify reported adjusted operating income of \$28.5 million, up 33.1% year over year. Adjusted operating margin remained flat on a year-over-year basis at 6%.

Balance Sheet & Cash Flow

As of Dec 31, 2019, Shopify ended the reported quarter with cash, cash equivalents and marketable securities balance of \$2.455 billion compared with \$2.667 billion as of Sep 30, 2019.

The company generated cash from operations of \$70.6 million during the year ended Dec 31, 2019, compared with \$9.3 million as of Dec 31, 2018.

Guidance

For first-quarter 2020, Shopify projects revenues in the range of \$440-\$446 million. In the first quarter, the company anticipates adjusted operating loss to be in the range of \$30 to \$34 million.

For full-year 2020, Shopify projects revenues in the range of \$2.13-\$2.16 billion. Shopify anticipates adjusted operating loss for fiscal 2019 to be in the range of \$0-\$20 million.

Quarter Ending **12/2019**

Report Date	Feb 12, 2020
Sales Surprise	4.75%
EPS Surprise	86.96%
Quarterly EPS	0.43
Annual EPS (TTM)	0.79

Recent News

On **Feb 21, 2020**, Shopify announced that it is joining Facebook's ambitious crypto-currency venture, Libra. The company is becoming a member of the Libra Association, in a bid to co-develop a payment network which makes money transfer easy to support both merchants and consumers, and facilitate commerce.

On **Dec 3, 2019**, Shopify announced its merchants set a high-record by achieving \$2.9 billion in sales on Black Friday/Cyber Monday weekend. This indicates year-on-year growth of 60%.

On **Nov 5, 2019**, Shopify announced launch of Shopify Email, a new email marketing tool to aid merchants in enhancing email marketing campaigns with templates, campaign analytics and brand asset importing functionalities.

On **Oct 17, 2019**, Shopify announced the closure of the acquisition of 6 River Systems, Inc. The deal is anticipated to boost growth of the company's fulfillment network.

On **Sep 30, 2019**, Shopify announced integration of its commerce platform with Microsoft Advertising to empower merchants with more digital ad campaigns to boost sales.

On **Sep 17, 2019**, Shopify rolled out new features on its platform with an aim to aid vendors sell hemp-derived and hemp Cannabidiol (CBD) products brick-and-mortar or online retail locations.

Valuation

Shopify shares are up 11.8% in the past six-month period and 81.5% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector are down 13.3% and 11.1% in the past six-month period, respectively. Over the past year, the Zacks sub-industry and the sector are down 23.6% and 6.2%, respectively.

The S&P 500 index is down 16.2% in the past six-month period and 10.6% in the past year.

The stock is currently trading at 18.87X forward 12-month sales, which compares to 4.53X for the Zacks sub-industry, 2.8X for the Zacks sector and 2.64X for the S&P 500 index.

Over the past three years, the stock has traded as high as 30.22X and as low as 7.75X, with a 3-year median of 12.77X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$321 price target reflects 16.03X forward 12-month sales.

The table below shows summary valuation data for SHOP

Valuation Multiples - SHOP					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	18.87	4.53	2.80	2.64
	3-Year High	30.22	11.42	3.58	3.44
	3-Year Low	7.75	4.53	2.62	2.64
	3-Year Median	12.77	7.15	3.19	3.15
P/B TTM	Current	14.45	4.22	3.96	3.34
	3-Year High	21.19	7.06	5.39	4.56
	3-Year Low	6.85	4.16	3.57	3.34
	3-Year Median	10.92	5.66	4.53	3.92
EV/Sales TTM	Current	26.06	4.58	3.30	2.48
	3-Year High	38.15	10.61	4.43	3.46
	3-Year Low	10.92	4.58	3.05	2.48
	3-Year Median	16.81	6.81	3.77	3

As of 03/12/2020

Industry Analysis Zacks Industry Rank: Top 36% (91 out of 253)



Top Peers

Autohome Inc. (ATHM)	Outperform
eBay Inc. (EBAY)	Outperform
ANGI Homeservices Inc. (ANGI)	Neutral
Etsy, Inc. (ETSY)	Neutral
Square, Inc. (SQ)	Neutral
Wix.com Ltd. (WIX)	Neutral
Zillow Group, Inc. (ZG)	Neutral
Groupon, Inc. (GRPN)	Underperform

Industry Comparison Industry: Internet - Services				Industry Peers		
	SHOP Underperform	X Industry	S&P 500	EBAY Outperform	GRPN Underperform	WIX Neutral
VGM Score	C	-	-	D	C	D
Market Cap	43.57 B	510.20 M	17.38 B	26.29 B	418.72 M	5.22 B
# of Analysts	24	3	13	7	3	9
Dividend Yield	0.00%	0.00%	2.51%	1.94%	0.00%	0.00%
Value Score	F	-	-	D	C	F
Cash/Price	0.05	0.18	0.05	0.10	1.20	0.11
EV/EBITDA	-683.45	4.12	10.90	10.63	-1.11	-114.09
PEG Ratio	49.47	1.55	1.54	0.96	NA	2.70
Price/Book (P/B)	14.45	1.84	2.35	9.16	1.06	25.13
Price/Cash Flow (P/CF)	NA	16.05	9.60	9.89	3.11	NA
P/E (F1)	1,831.66	21.28	13.98	10.77	15.83	94.44
Price/Sales (P/S)	27.61	2.08	1.89	2.43	0.19	6.86
Earnings Yield	0.06%	1.70%	7.07%	9.29%	6.76%	1.06%
Debt/Equity	0.00	0.11	0.70	2.52	0.54	1.73
Cash Flow (\$/share)	-0.60	0.13	7.01	3.34	0.24	-0.25
Growth Score	A	-	-	C	B	A
Hist. EPS Growth (3-5 yrs)	NA%	24.13%	10.85%	-2.66%	NA	NA
Proj. EPS Growth (F1/F0)	-31.25%	12.81%	5.99%	8.38%	-64.10%	-5.22%
Curr. Cash Flow Growth	85.89%	5.64%	6.15%	8.64%	-29.11%	-2,949.32%
Hist. Cash Flow Growth (3-5 yrs)	NA%	17.68%	8.52%	-6.76%	11.55%	11.92%
Current Ratio	8.68	1.62	1.24	1.16	1.08	1.72
Debt/Capital	0.00%	9.94%	42.57%	71.58%	35.23%	63.40%
Net Margin	-7.91%	-4.91%	11.64%	16.54%	-1.01%	-11.35%
Return on Equity	-2.69%	-3.50%	16.74%	50.71%	3.39%	-27.21%
Sales/Assets	0.55	0.60	0.54	0.54	1.50	0.75
Proj. Sales Growth (F1/F0)	37.35%	13.39%	3.54%	-10.08%	-38.63%	25.12%
Momentum Score	C	-	-	D	C	F
Daily Price Chg	-10.54%	-7.84%	-10.03%	-5.17%	-13.68%	-8.92%
1 Week Price Chg	1.89%	-0.24%	-0.67%	5.05%	-17.91%	1.66%
4 Week Price Chg	-29.12%	-22.63%	-28.22%	-11.19%	-75.05%	-28.64%
12 Week Price Chg	-3.89%	-20.69%	-25.63%	-8.35%	-67.53%	-13.57%
52 Week Price Chg	81.42%	-34.16%	-16.72%	-9.13%	-78.21%	-4.16%
20 Day Average Volume	2,741,512	114,320	3,061,271	13,426,923	22,501,320	1,130,572
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-113.59%	0.00%	-0.32%	2.29%	-140.00%	-19.33%
(F1) EPS Est 12 week change	-112.70%	-1.19%	-0.65%	7.85%	-140.00%	-19.11%
(Q1) EPS Est Mthly Chg	-132.27%	0.00%	-0.62%	3.73%	-433.33%	-7.89%

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	F
Growth Score	A
Momentum Score	C
VGM Score	C

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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