

Shopify, Inc.

USF Student Managed Investment Fund	Recommendation	Current Price	1-Yr Target Price
Analysts: Andres Nader, Quan Nguyen, Jose Ortiz, and Sam Rodas	BUY	68.86	80.82

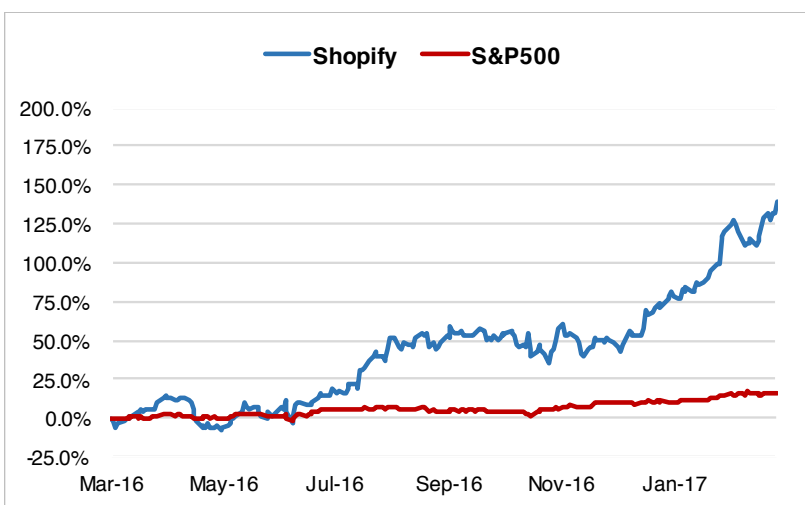
Sector Information Technology
Industry Internet Software & Services

Summary Shopify provides a subscription-based, e-commerce platform that helps small and medium-sized businesses set up, manage, and grow their online stores.

Key Data

IPO Date May 2015 **Market Cap** 6.2B **52-Week Range** \$24.96 - \$68.92 **P/S** 13.8 **P/B** 14.0

Price Performance



Competitive Moat

- Capabilities to serve merchants of all sizes, from entrepreneurs to large enterprises
- Strategic and exclusive partnerships with tech companies and business celebrities
- Consistently improving brand image that is superior to other white-label e-commerce platforms

Investment Thesis

- Despite e-commerce's strong historical growth, the industry is still in its early stages, indicating an opportunity for it to continue growing and for new players such as Shopify to outpace industry leaders
- As the only platform among its peers with a multi-channel approach and along with a robust partner ecosystem, Shopify will be continue to attract and retain merchants
- Being a small company in a largely untapped market, Shopify has tremendous upside potential as proven by its historical growth

Risks

- History of operating and net losses
- Cyber attacks
- Reliance on a single supplier to support Shopify Payments
- Dependence on strategic relationships with third parties

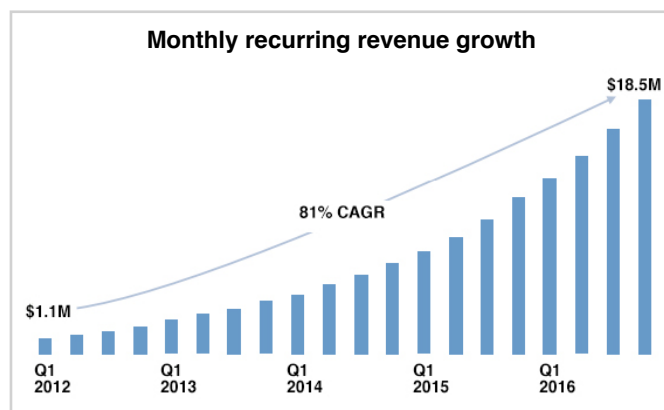
Business Summary

Shopify allows businesses, or merchants, to create white-label online stores and manage their online operations through a single platform. The Shopify platform provides a comprehensive suite of back-office software that enables merchants to design their online stores, manage products, process orders and payments, and much more. Shopify focuses on serving small- to medium-sized businesses. Its intuitive platform removes the need for any coding experience or technical knowledge. Shopify currently powers over 375,000 merchants in approximately 150 countries.

Shopify has two main revenue streams: a recurring subscription component called *subscription solutions* and a merchant success-based component called *merchant solutions*.

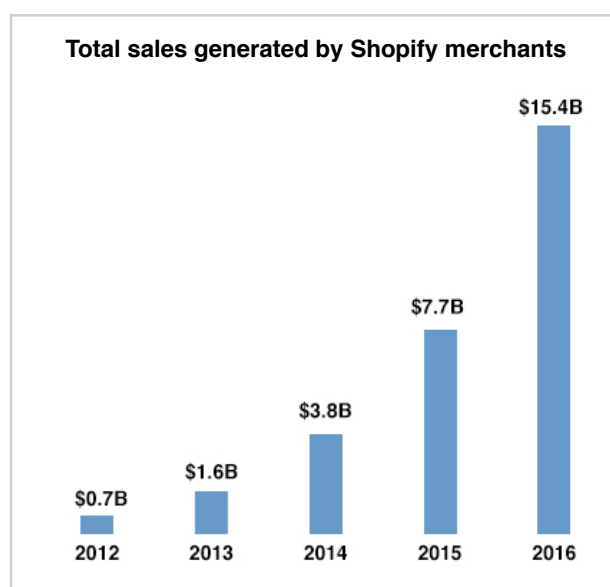
Subscription Solutions

Shopify generates the majority of its subscription solutions revenues through the sale of subscriptions to its platform. Merchants can opt for different pricing plans depending on their needs. Offering different service and pricing levels allows merchants to scale and grow without leaving the Shopify platform. In addition to revenues from subscriptions to the platform, Shopify generates subscription solutions revenues from the sale of store themes, apps and the registration of domain names.



Merchant Solutions

Shopify offers a variety of merchant solutions that are designed to add value to businesses using its platform. The majority of merchant solutions revenues come from payment processing fees from *Shopify Payments*, a payment processing service that allows merchants to accept and process payment cards. In addition, Shopify generates merchant solutions revenues from referral fees from partners, sales of point-of-sale hardware, *Shopify Shipping*, and *Shopify Capital*. *Shopify Shipping* allows merchants to buy and print shipping labels and track orders directly within the Shopify platform. *Shopify Capital* is a merchant cash advance program that offers financing to merchants to grow their businesses.



Investment Rationale

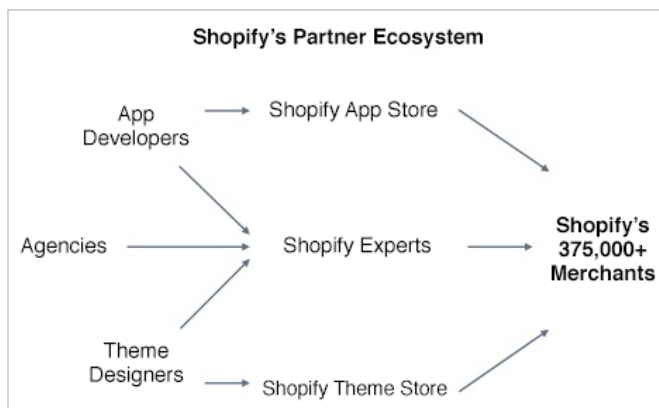
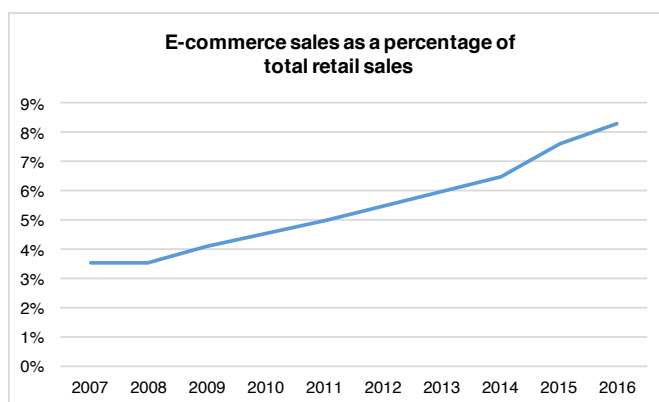
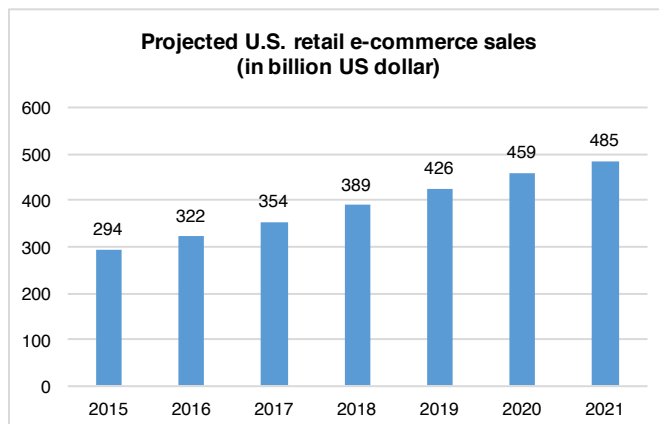
E-commerce has been growing fast, but the industry is still in its early stages

E-commerce sales' strong growth is expected to continue across our investment horizon. Worldwide e-commerce sales reached \$22 trillion in 2016 and are estimated to reach \$27 trillion in 2020. However, e-commerce sales only represent 8.3% of total retail sales in 2016. This unique combination of fast-growth and low market share indicates an enormous opportunity for the industry to continue growing and for new players such as Shopify to outpace industry leaders.

As the need of small to medium-sized businesses to build an e-commerce operation increase, they will look for a platform that is easy to use and offers the most capabilities. Shopify is consistently ranked as one of the most intuitive e-commerce platforms that offers powerful features that can serve businesses of all sizes.

Shopify's multi-channel strategy and ecosystem will help attract and retain merchants

Shopify began its multi-channel strategy in 2015 and has remained the only company among its peers with this approach. Shopify merchants have the ability to sell their products on online channels such as Facebook, Pinterest, and Twitter, as well as offline through Shopify's Point-of-Sale system. This multi-channel strategy will attract merchants to the Shopify platform, bolster their sales, and consequently increase Shopify's top-line. With a robust partner ecosystem consisting of thousands of app developers, agencies, and designers, Shopify merchants have access to business guidance and a constant stream of new apps and themes. These resources will help grow and retain Shopify merchants.



Shopify, Inc.

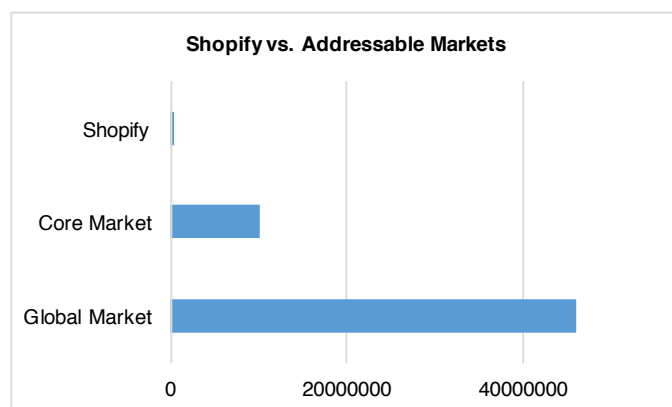
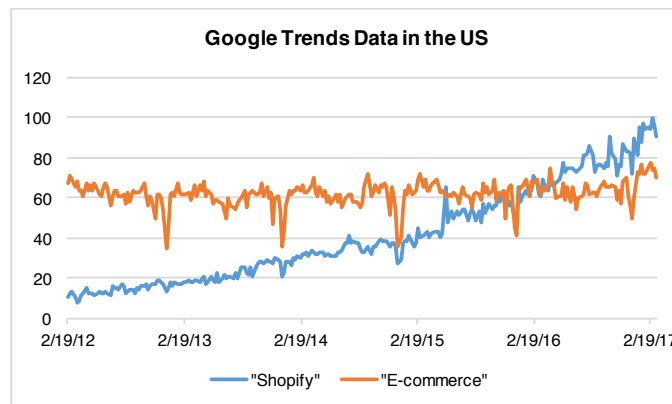
Investment Rationale (Cont.)

Huge upside potential as Shopify is a small company in a largely untapped market

Shopify has grown to be a leading brand among white-label e-commerce platforms. The company's revenues grew at a consistent 100% compound annual growth rate over the past five years.

Despite its strong historical growth, Shopify is still a small company with a market cap of 6.2B. Shopify's merchant base of 375,000 merchants is small compared that of its larger competitor Ecwid, which has a merchant base of 1 million. Shopify estimated its core market at 10 million and global market at 46 million. This means the company has claimed only 3.8% and 0.8% of its core market and global market, respectively.

Because of its size and B2B model, Shopify remains underexposed to mass media despite its strong growth history. For example, on January 5, 2017, Shopify stock rose 8% after rumor of a partnership with Amazon surfaces. This partnership plan was already announced in September 2015 on the company's website. Incidents like this imply that many investors are unaware of the company, creating an attractive entry point.



Competitive Moat

Capable to Serve Merchants of All Sizes

Shopify’s platform has the capabilities to serve businesses of all stages, from entrepreneurs to large enterprises. The company offers different plans that meet the needs of different merchants according to their stages. In 2016, Shopify rolled out Shopify Plus to cater large enterprises and had since attracted customers such as Tesla Motors, Google, and the LA Lakers.

Exclusive Partnerships with Companies

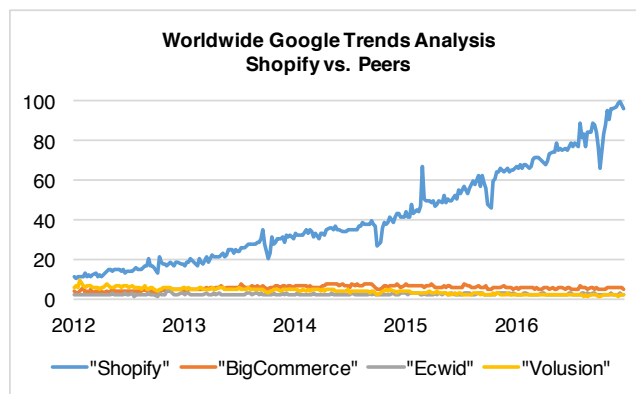
Shopify has several exclusive partnerships with large technology companies and business celebrities. For example, the Facebook partnership gives merchants the opportunity to directly sell to and communicate with Facebook users. The partnership with Uber allows Shopify merchants to deliver orders to local customers quickly.

Shopify also partners with business celebrities to host one of the world’s biggest entrepreneurial competitions called *Build a Business*. Over the past 6 years, Shopify’s competitions have helped inspire over 100,000 new businesses that have sold millions of dollars in products.



Superior Brand Image

Compared to its direct competitors, Shopify has built a strong brand popularity in the cloud e-commerce industry. As indicated by Google Trends’ analysis, there is a large gap between Shopify and its key competitors for Google searches made by merchants and stakeholders searching for e-commerce solutions. The firm also has a presence in multiple social channels. In 2016, Shopify had over 16M visits on its blog, 1.6M Facebook friends, and 233K email subscribers. Shopify’s new merchant acquisition will benefit from this market leading exposure and merchant awareness.



Competition

Shopify is the leading pure-play e-commerce platform in what is becoming a very competitive market. The company has three major competitors, none of which are publicly traded: BigCommerce, Volusion, and Ecwid.

BigCommerce is the most closely related alternative to Shopify with approximately 100,000 stores as users. Like Shopify, BigCommerce offers mostly the same e-commerce tools needed to help make a merchant successful. However, BigCommerce's presence in mobile and online store is much smaller compared to Shopify. Shopify has over 1400 apps and 377,000 online stores, while BigCommerce has 250 apps and 95,000 online stores.



Volusion is a popular alternative to Shopify with approximately 40,000 stores as users. Volusion's e-commerce features are similar to those of Shopify. However, the Volusion platform has many drawbacks: limited bandwidth on every plan, a limited number of products, poor design options, and a limited number of apps available.



Ecwid is not a direct competitor to Shopify, but can still be considered an alternative. Ecwid doesn't allow its customers to build stores with e-commerce abilities, instead allows its customers to add stores to websites already created. Ecwid works as a widget for e-commerce and has approximately 1 million store users. The major drawbacks with Ecwid include limitations with plans offered, limited or no merchant support, limited apps, and limited with search engine optimization.



Management

Shopify's management team consists of 10 executives. The majority has been with the company for more than 5 years. Tobias Lütke, Shopify's co-founder, has led the company as its CEO since 2008. Lütke's previous experience includes working on the core team of the Ruby on Rails framework and founding several popular open source libraries such as Active Merchant. Other executives' past experience include holding leadership positions at companies such as eBay, EMC Corp., IBM, and Netflix. Shopify's board of directors consists of 5 individuals who are elected annually by shareholders.

Risks

History of operating and net losses

Since Shopify's IPO in 2015, it has taken losses and deficits in attempts to focus on growth. Investment expenditures make it harder for the company to achieve profitability. Additionally, the company has potential to incur more operating expenses as it grows further. Regardless of historical losses, the company's continued commitment investing demonstrates the potential for high growth.

Cyber attacks

Shopify is part of an industry that is prone to cyber attacks. Security breaches of any sort puts at risk the company's data and merchants' data, which could adversely affect the reputation of the company. Previously, the company has been subject to attacks by hackers that take internet services offline by overloading the company's service, Distributed Denial of Service. As cyber security risks increase, Shopify continues to be committed to investing in protection against threats.

Reliance on a single supplier to provide the technology for Shopify Payments

Stripe Inc., is the provider for the technology that makes Shopify Payments function. A termination with Stripe's agreement would create substantial expenses in finding and integrating an alternative payment supplier. Shopify is also dependent on Stripe's technology to process customers' cards and protect their data. Stripe is a reputable supplier of payment technology that serves large corporations such as Under Armour, Adidas, Best Buy, and Target.

Dependence on strategic relationships with third parties

The company's growth is contingent on relationships with third party app developers, theme designers, referral sources, resellers, and other partners. These partners may terminate the relationships with the company at any time, negatively impacting business and operations. However, Shopify has managed to have secure and reliable relationships with many of its third party providers.

Valuation

EV/EBITDA					
Inputs	2017E	2018E	2019E	2020E	2021E
Operating Income (EBIT)	(14)	27	41	60	102
Stock-Based Compensation	55	72	95	122	155
Depreciation	25	36	43	50	61
EBITDA	66	135	179	233	318
Multiple	100	80	70	60	50
Enterprise Value	6,571	10,824	12,506	13,967	15,922
Plus Cash	395	426	429	431	432
Market Cap	6,966	11,249	12,935	14,397	16,354
Shares Outstanding	91	98	106	114	123
Price Target	\$ 76.79	\$ 114.81	\$ 122.24	\$ 125.98	\$ 132.51

EV/Sales					
Inputs	2017E	2018E	2019E	2020E	2021E
Total Revenues	609	822	1,096	1,437	1,862
Multiple	12	12	10	9	8
Enterprise Value	7,302	9,860	10,961	12,932	14,898
Plus Cash	395	426	429	431	432
Market Cap	7,697	10,285	11,389	13,363	15,330
Shares Outstanding	91	98	106	114	123
Price Target	\$ 84.85	\$ 104.97	\$ 107.63	\$ 116.93	\$ 124.21

Weighted Average of EV/EBITDA AND EV/Sales					
Inputs	2017E	2018E	2019E	2020E	2021E
EV/EBITDA	6966	11249	12935	14397	16354
Weight	50%	50%	50%	50%	50%
EV/Sales	7697	10285	11389	13363	15330
Weight	50%	50%	50%	50%	50%
Weighted Market Cap	7332	10767	12162	13880	15842
Shares Outstanding	91	98	106	114	123
Equity Value Per Share	\$ 80.82	\$ 109.89	\$ 114.94	\$ 121.46	\$ 128.36

Our one-year target price of \$80.82 is based on on the weighted average of EV/EBITDA and EV/Sales multiples, which represents a 17% upside to today's share price. We believe that this premium is reasonable given our expectation of above average growth relative to consensus and management estimates. We believe that this target price and multiple are warranted given (1) SHOP's leading cloud-based commerce platform for SMBs, (2) large market opportunity, (3) significant customer momentum and growth, and (4) highly extensible platform / ecosystem, and accordingly initiate a Buy rating.

Valuation

	Fiscal 2016 by Quarter			Fiscal 2017 by Quarter			Fiscal 2018 by Quarter			Fiscal 2019 by Quarter			Fiscal Year End December									
	Mar 16	Jun 16	Sep 16	Mar 17	Jun 17	Sep 17	Mar 18	Jun 18	Sep 18	Mar 19	Jun 19	Sep 19	Dec 19	2014A	2015A	2016A	2017E	2018E	2019E			
SHOPFY (SHOP) INCOME STATEMENT	Fiscal year ends in December. USD in millions, unless otherwise specified																					
Revenue	72.7	86.6	99.6	130.4	122.5	136.3	151.9	197.8	163.5	184.7	203.4	268.0	195.1	224.9	249.9	329.4	105	205.2	389.3	608.5	821.6	999.2
Subscription Solutions	38.7	43.7	49.8	56.6	59.5	64.2	72.0	82.6	85.1	88.8	94.1	107.8	108.2	110.1	112.4	128.4	66.7	112	188.6	278.3	375.8	459.16
Merchant Solutions	34	43	49.7	74	63.0	72.2	79.8	115.4	78.4	96.2	111.1	160.7	90.5	116.2	138.6	200.4	38.4	93.3	200.7	330.5	446.4	545.68
Gross profit	39.4	46.3	52.7	68.4	66.4	73.2	82.2	101.7	93.3	102.3	112.1	139.5	118.9	129.5	138.7	173.8	62.1	111.4	206.7	323.5	447.3	560.94
% of revenue	54.2%	53.5%	52.9%	52.5%	54.2%	53.7%	54.1%	51.4%	57.0%	55.4%	54.6%	52.1%	61.0%	57.6%	55.5%	52.8%	59.1%	54.3%	53.1%	53.4%	54.8%	56.7%
Operating expenses																						
Research and development	11.4	13.5	15.1	19	20.0	23.0	24.5	27.9	24.7	28.8	30.6	37.0	28.3	33.4	35.4	44.6	23.1	33.3	59	95.3	121.0	141.68
% of revenue	15.7%	15.6%	15.2%	14.6%	16.3%	16.8%	16.1%	14.1%	15.1%	15.6%	14.9%	13.8%	14.5%	14.8%	14.2%	13.5%	22.0%	16.2%	15.1%	15.8%	14.8%	14.3%
Sales and marketing	27.4	28.4	31.4	37.6	41.1	42.5	44.1	52.7	50.8	53.1	54.9	68.5	58.3	61.5	63.3	81.4	45.2	69	124.8	180.4	227.3	264.48
% of revenue	37.7%	32.8%	31.5%	28.8%	33.6%	31.2%	29.1%	26.6%	31.0%	28.8%	26.7%	25.5%	29.9%	27.4%	25.3%	24.7%	43.1%	33.6%	32.0%	30.1%	28.0%	26.8%
General and administrative	6.5	7.7	8.4	12.6	13.6	14.8	16.1	17.5	16.3	17.1	18.5	19.6	18.4	18.8	20.3	21.0	8.7	15.7	35.1	62.0	71.5	78.472
% of revenue	8.9%	8.9%	8.4%	9.7%	11.1%	10.9%	10.6%	8.8%	10.0%	9.3%	9.0%	7.3%	9.4%	8.4%	8.1%	6.4%	8.3%	7.7%	9.0%	10.4%	8.9%	8.1%
Total operating expenses	45.3	49.5	54.9	69.2	75.2	80.2	85.5	98.8	92.4	99.0	104.8	126.4	112.7	120.1	127.3	160.4	77	118.1	218.9	339.7	422.5	520.48
Operating margin	-5.9	-3.2	-2.2	-0.8	-8.2	-7.1	-2.6	3.6	1.6	3.3	8.2	14.5	6.3	9.4	11.4	13.4	-15	-6.7	-12.1	-14.3	27.5	40.5
Stock based compensation expense	-8.1%	-3.7%	-2.2%	-0.6%	-6.7%	-5.2%	-1.7%	1.8%	1.0%	1.8%	4.0%	5.4%	3.2%	4.2%	4.6%	4.1%	-14.3%	-3.3%	-3.1%	-2.9%	3.0%	4.0%
% of revenue	3.5	5.1	6.5	8.1	11	12.7	14.6	16.7	17.2	17.7	18.2	18.7	23.1	23.6	24.1	24.6	4.4	8.2	23.1	55	71.8	95.4
Interest and other, net	4.8%	5.9%	6.5%	6.2%	9.0%	9.3%	9.6%	8.4%	10.5%	9.6%	8.9%	7.0%	11.8%	10.5%	9.6%	7.5%	4.2%	4.0%	5.9%	9.1%	9.0%	9.9%
Pretax income	0.8	0.2	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	-0.7	-1	1.8	1.6	1.6	1.6
Effective tax rate	-5.1	-3	-1.8	-0.4	-7.8	-6.7	-2.2	4.0	2.0	3.7	8.6	14.9	6.7	9.8	11.8	13.8	-15.7	-7.7	-10.3	-12.7	29.1	42.062
Pro forma net income	0%	0%	0%	0%	0.0	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Pro forma net margin	-5.1	-3	-1.8	-0.4	-7.8	-6.7	-2.2	4.0	2.0	3.7	8.6	14.9	6.7	9.8	11.8	13.8	-15.7	-15.7	-10.3	-12.7	29.1	42.062
Pro forma EPS	-7.1%	-3.5%	-1.8%	-0.3%	-6.4%	-4.9%	-1.4%	2.0%	1.2%	2.0%	4.2%	5.6%	3.4%	4.4%	4.7%	4.2%	-14.9%	-3.8%	-2.7%	-2.7%	3.2%	4.2%
	-0.06	-0.04	-0.02	0.00	-0.09	-0.07	-0.02	0.04	0.02	0.04	0.09	0.15	0.07	0.10	0.12	0.14	-0.4	-0.13	-0.12	-0.14	0.30	0.4293

Valuation

SHOPIFY (SHOP) BALANCE SHEET	Fiscal 2016 by Quarter			Fiscal 2017 by Quarter			Fiscal 2018 by Quarter			Fiscal 2019 by Quarter			Fiscal Year End December											
	Mar 16	Jun 16	Sep 16	Dec 16	Mar 17	Jun 17	Sep 17	Dec 17	Mar 18	Jun 18	Sep 18	Dec 18	Mar 19	Jun 19	Sep 19	Dec 19	2014A	2015A	2016A	2017E	2018E	2019E		
Assets																								
Current assets																								
Cash and cash equivalents	84	68.1	187.4	84	76.1	76.3	72.5	86.7	79.3	90.1	93.1	117.1	82	92.8	95.8	119.8	42	110.1	84	86.7	117.1	112.8		
Marketable securities	105.6	111.5	212.9	308.4	308.4	308.4	308.4	308.4	308.4	308.4	308.4	308.4	308.4	308.4	308.4	308.4	17.7	80.1	308.4	308.4	308.4	308.4	308.4	
Accounts receivable, net of ADA	6.5	9.1	7.7	9.6	12.2	10.5	10.1	13.1	12.6	12.2	13.5	17.6	13.3	12.9	14.2	18.3	7.2	6.1	9.6	13.1	17.6	6.8		
Merchant cash advances receivables		9.1	11.9		12	12.1	12.3	12.4	12.8	12.8	12.9	12.9	13.3	13.3	13.4	13.4			11.9	12.4	12.9	0.5		
Prepaid expenses and other assets	7.1	7.1	10.3	9	9.3	9.3	9.5	9.9	10.2	10.2	10.5	10.9	10.7	10.7	11	11.4	1.5	6.2	9	9.9	10.9	6.7		
Total current assets	203.2	195.9	427.4	422.9	418	416.7	412.7	430.4	423.3	433.7	438.4	466.9	427.7	438.1	442.8	471.3	68.4	202.5	422.9	430.4	466.9	435.2		
Long-term assets																								
Property, plant and equipment, net	34.6	39.1	42.8	45.7	47.7	49.2	50	50.1	51	51.5	52.1	52.3	51.7	52.2	52.8	53	21.7	33	45.7	50.1	52.3	33.7		
Goodwill	2.4	9.3	9.3	15.5	15.5	15.5	15.5	15.5	15.5	15.5	15.5	15.5	15.5	15.5	15.5	15.5	2.4	2.4	15.5	15.5	15.5	15.5		
Intangible assets, net	5.2	6.8	6.9	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	2.7	5.8	6.4	6.4	6.4	6.4		
Total assets	245.3	251.1	486.3	490.6	487.6	487.8	484.7	502.5	496.2	507.2	512.4	541.2	501.3	512.2	517.5	546.2	95.2	243.7	490.6	502.5	541.2	490.8		
Liabilities and stockholders' equity																								
Liabilities																								
Current liabilities																								
Accounts payable	27.1	32.3	42.3	45.1	49.7	55.2	53.9	66.9	61.8	68.8	66.4	81.7	63.8	70.8	68.4	83.7	12.5	23.7	45.1	66.9	81.7	25.7		
Deferred revenue, current portion	14.5	16.5	18.3	20.2	21.8	23.9	25.6	28.2	28.3	31	33.3	36.7	29.3	32	34.3	37.7	6.8	12.7	20.2	28.2	36.7	13.7		
Lease incentives, current portion	0.9	1.1	1.2	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	0.5	0.8	1.3	1.3	1.3	1.3		
Total current liabilities	42.5	49.8	61.9	66.5	72.8	80.4	80.9	96.5	91.5	101.1	101	119.7	94.4	104.1	104	122.7	19.8	37.2	66.5	96.5	119.7	40.7		
Long-term liabilities																								
Deferred revenues, net of current portion	0.8	0.8	0.9	0.9	1.1	1.2	1.3	1.3	1.4	1.6	1.7	1.7	1.9	2.1	2.2	2.2	0.4	0.7	0.9	1.3	1.7	1.2		
Lease incentives	11	11.7	12.1	12.6	12.3	12	11.7	11.4	11.1	10.8	10.5	10.2	11.6	11.3	11	10.7	7.3	10.5	12.6	11.4	10.2	11		
Total liabilities	54.3	62.4	74.8	80.1	86.2	93.6	93.9	109.2	104	113.5	113.2	131.6	107.9	117.5	117.2	135.6	27.5	48.4	80.1	109.2	131.6	52.9		
Total stockholders' equity	191	188.8	411.5	410.5	401.4	394.2	390.8	502.5	392.2	393.7	399.3	409.5	393.3	394.8	400.4	410.6	-19.3	195.3	410.5	393.3	409.5	196.4		
Total liabilities and stockholders' equity	245.3	251.1	486.3	490.6	487.6	487.8	484.7	502.5	496.2	507.2	512.4	541.2	501.2	512.3	517.6	546.2	95.2	243.7	490.6	502.5	541.2	249.3		