

# Adding Shopify to your Cart

## The “Operating System” of Retail

We're excited to initiate you in Shopify, the leading commerce platform that helps merchants operate and sell products online and offline. This stock replaces Salesforce.com (CRM) in our Flagship portfolio.

### SHOPIFY (SHOP)

Industry	Software
Stock Price	\$914.02
Market Cap	\$111.8 billion
Price Target	~\$1500 (+64%)

## Investment Thesis

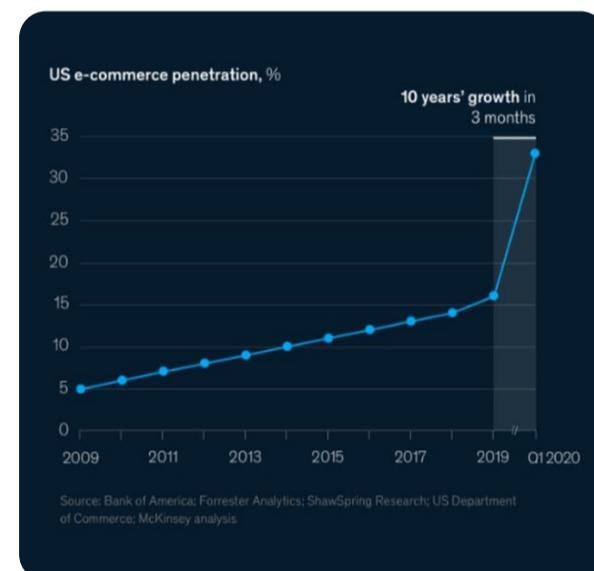
**We believe Shopify is the “operating system” of modern retail, and is positioned to capitalize tremendously on the recent step function increase in e-commerce penetration globally.**

**First, we think e-commerce penetration has jumped 10 years forward in 90 days’ time** as a result of the COVID-19 pandemic. This shift seems unlikely to reverse course, even as the country re-opens, due to an accelerated pace of brick & mortar store closures that will force even more commerce online. We think e-commerce industry sales can grow 20%+ per year.

This shift validates Shopify’s massive total addressable market (TAM). Shopify’s gross merchandise value (GMV), or total sales by Shopify merchants, had only ~2% market share in 2019. GMV should compound at 30%+ per year for the next 3-5+ years as its growing suite of tools and marketplace integrations serve as a tailwind to new customer growth and merchant success.

**Next, we believe Shopify’s revenue can grow 35-40%+ per year for the next 3-5+ years.** Shopify makes money from both subscription solutions (recurring software revenue) and merchant solutions (transaction based take rate), but the majority is merchant solutions (where we think the largest opportunity lies). The company is seeing growing adoption of new merchant solutions (like Shopify Fulfillment Network, Shopify Balance business accounts, and Shop Pay Installments), which are significantly expanding the opportunity per merchant. These services should also drive Shopify’s take rate of GMV higher over time.

**Expanding partnerships and international investments are additional revenue opportunities.** Shopify only began actively investing in international markets in 2018, and international is only ~30% of Shopify’s merchant base today (vs. ~75% of total global GMV), hence we see meaningful upside. Partnerships have also been an impressive business development at Shopify in recent months, and a validation of the dominance of its platform. From TikTok (helping over 1M merchants create and run video campaigns) to Alipay (enabling US merchants to accept payments from over 1B users in China), Shopify is helping merchants reach their customers in ways not available on any other platform.



**Strong unit economics and increasing scale should support 30%+ operating margins over time.**

SHOP's customer acquisition cost (CAC) is significantly lower than that of SMB-focused peers due to its customer acquisition funnel (word-of-mouth and digital advertising vs. large direct salesforce). And while its lifetime value (LTV) of customers is average (due to higher churn associated with SMB merchants that often go out of business), over time its LTV/CAC should improve as the company moves up-market with Shopify Plus and ramps newer merchant solution products (better retention and gross margin).

**The biggest risk with owning SHOP today is admittedly valuation.** The stock is trading at ~28x forward EV/sales vs. peers' averaging closer to 20x. While this is arguably justified by the faster growth rates SHOP exhibits and its best-in-class acquisition model, we expect valuation to be a sticking point for many investors (as it has been for many years). Ironically, we believe this is part of the opportunity. Given the lack of viable competitors and the massive market opportunity, we believe SHOP is well-positioned to continue beating and raising sales estimates, growing into its valuation over time.

**In summary, we believe SHOP could be the next Amazon or Netflix:** a rapidly-growing, founder-led company in a massive and growing market, but which is perennially undervalued by investors due to concerns about near-term valuation; concerns which underestimate the longevity of SHOP's top-line growth algorithm and the pull-forward impact of COVID-19 on e-commerce penetration more broadly.

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## Exited Position: CRM

**Salesforce.com (CRM)** is the global leader in cloud-based software for customer relationship management. The company delivers its services via internet browsers and on mobile devices, and they're highly integrated with other frequently-used enterprise applications.

**Original thesis:** "Salesforce.com is the undisputed leader in cloud-based CRM software, with 20% market share in a massive and growing market. The AI-based CRM market should expand to over \$1 trillion by 2021, and the company will take share in that market. The company has strong recurring free cash flow from its sticky, high-margin subscription revenue model... should see margins and cash flow improve."

**What changed: Valuation expanded materially such that we now see a better risk/reward in Shopify.**

The business remains incredibly strong, but CRM's forward enterprise value to sales (EV/sales) ratio rose from ~6x at our initiation in Feb 2018 and at the mid-March COVID lows (in line with its historical average) to ~10x recently. This is the most expensive valuation for CRM in decades and one we're not as excited to pay, especially with small/mid cap software valuations having risen materially (adding incremental risk to CRM's acquisition-driven growth algorithm).

**Our action: We exited our position in mid-November up +124% (+34% annualized return)** since we initiated the investment for Titan clients in February 2018. We're very pleased with this outcome and would consider re-initiating the position if the risk/reward becomes very attractive again in the future.

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If you have any questions, please don't hesitate to email us at [research@titanvest.com](mailto:research@titanvest.com).



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