

Square, Inc. (SQ)

\$83.33 (As of 02/28/20)

Price Target (6-12 Months): **\$87.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 11/25/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: F

Growth: B

Momentum: F

Summary

Square reported impressive fourth quarter results wherein both earnings and revenues have reflected year over year growth on the back of solid gross payments volume. Moreover, the company's seller ecosystem which helps in strengthening relationship with sellers, contributed well to the payment volume as well as the top-line growth. Also, robust performance by product lines such as Square Terminal, Cash Card, Square Register and Square Capital drove the top-line growth further. Additionally, growing adoption of Cash App in the bitcoin space remained a tailwind for Square's business growth. The stock has outperformed the industry it belongs to over a year. However, increasing product development expenses and costs related to Cash Card issuances are risks. Further, intensifying competition and foreign exchange fluctuations remain headwinds.

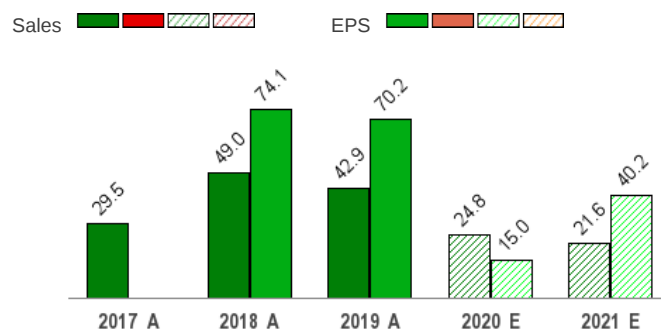
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$87.25 - \$54.41
20 Day Average Volume (sh)	8,981,726
Market Cap	\$35.8 B
YTD Price Change	33.2%
Beta	3.26
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Internet - Software
Zacks Industry Rank	Top 42% (106 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	15.0%
Last Sales Surprise	10.7%
EPS F1 Est- 4 week change	-24.3%
Expected Report Date	NA
Earnings ESP	-0.2%
P/E TTM	104.2
P/E F1	90.6
PEG F1	2.3
P/S TTM	7.6

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,599 E	1,833 E	1,934 E	1,964 E	7,154 E
2020		1,407 E	1,504 E	1,504 E	5,883 E
2019	959 A	1,174 A	1,266 A	1,313 A	4,714 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.23 E	\$0.29 E	\$0.34 E	\$0.37 E	\$1.29 E
2020	\$0.15 E	\$0.21 E	\$0.27 E	\$0.28 E	\$0.92 E
2019	\$0.11 A	\$0.21 A	\$0.25 A	\$0.23 A	\$0.80 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 02/28/2020. The reports text is as of 03/02/2020.

Overview

Headquartered in San Francisco, CA, Square, Inc. was incorporated in 2015. The company offers financial and marketing services through its comprehensive commerce ecosystem that helps sellers to start, run and grow their businesses.

We combine sophisticated software with affordable hardware to provide sellers powerful payment and point-of-sale solutions. The company provides payment and point-of-sale (POS) services, which include hardware and software to accept payments, streamline operations and analyze business information.

Square's payments and POS services include In-Person Payments, Online Payments, Square Cash, Square Register, Square Analytics, Square Appointments and Square App Marketplace. The company's financial services include Square Capital and Square Payroll.

Square reported total revenues of \$4.7 billion in 2019. The company earns revenues from transactions, subscription and services, hardware and bitcoin.

Transaction-based revenues (65.4% of total revenues in 2019) include transaction fees that sellers pay for managed payment solutions and services.

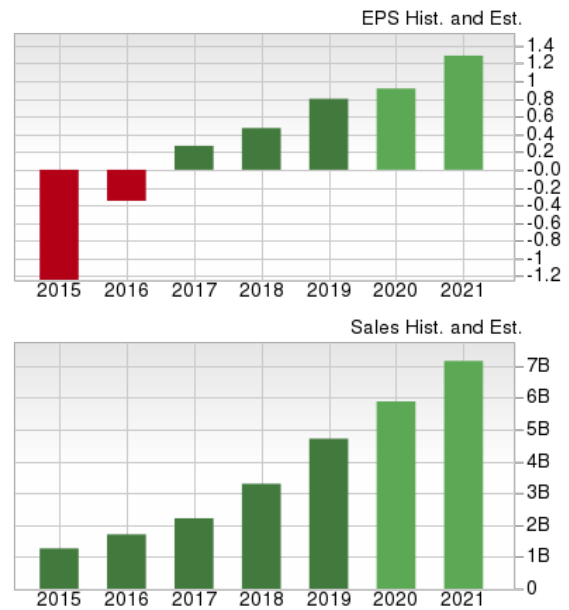
Subscription and services-based revenues (21.9%) include fees that sellers pay for a range of paid services-based products including Square Appointments, Gift Cards, Customer Engagement, Employee Management, Payroll, Instant Deposit, and other subscription and services-based products offered through Square Marketplace. A significant portion of the revenues comes from Square Capital that provides loans to pre-qualified sellers and Caviar, Square's food ordering service.

Hardware revenues (1.8%) are generated from sales of contactless readers, chip card readers and third-party peripherals which include cash drawers, receipt printers and barcode scanners. Square's hardware portfolio is comprised of Square Stand, Magstripe reader, Square Register and Square Terminal, and chip readers.

Bitcoin revenues (10.9%) are derived from total sales of bitcoin to customers. Cash App users can buy and sell bitcoins.

Geographically, the United States contributed almost 94.9% of revenues, while the rest came from International markets.

The company had approximately 3,835 employees worldwide as of Dec 31, 2019.



Reasons To Buy:

- ▲ Square differentiates itself by offering a **comprehensive commerce ecosystem** enabling sellers to combine software, hardware and payments services from several vendors. The company's managed payment solutions allow sellers to accept payment through a range of media such as magnetic stripe (a swipe), Near Field Communication (NFC), EMV (Europay, MasterCard, and Visa), online through Square Invoices, Square Virtual Terminal, or the seller's website. Square's powerful point-of-sale software and services help sellers manage locations, orders, inventory, employees, and payroll. It helps sellers grow their sales with customers; and gain access to business loans. The Square Capital service offers loans to sellers on the basis of their payment processing history. Caviar, the company's food ordering service, helps restaurants gain access to new customers and enhance sales without additional overhead. A technology focused approach has enabled the company to develop products and services that are unified, fast, self-serve, and reliable and we expect this to continue in the coming years. We believe the company's strong efforts toward expansion of its payment solutions portfolio will continue to drive its top-line growth and aid momentum in the growing market for online payment solutions.
- ▲ Square's **rate of growth has been impressive** since it started operations eight years back. The company serves millions of sellers across various industries such as food, retail and services, and geographies including the U.S., Japan, Australia and Canada. It processed \$106.2 billion of Gross Payment Volume (GPV) in 2019. The company has been doing well with larger and midmarket sellers. In fourth-quarter 2019, larger sellers contributed 55% to total GPV, up 33% from the year-ago quarter. The company's robust product portfolio is the key catalyst behind its improving GPV. The newly launched Square Reader SDK is a major positive. Additionally, API Platforms, Build with Square, Virtual Terminal, Instant Deposit and especially Square for Restaurants will continue to drive the GPV growth further.
- ▲ Square's **entry into bitcoin market** with CashApp product, is contributing well to the company's quarterly results. Further, Square's expanding global presence will continue to benefit its top-line growth. The introduction of CashApp and Instant Deposit in U.K. bodes well for the company's market position and it will continue to generate revenues.

Square's comprehensive commerce ecosystem, accelerated business growth and entry into bitcoin space remain major positives.

Reasons To Sell:

- ▼ Growth will continue to depend on the company's ability to differentiate. Square is **vulnerable to intense competition and changing technology, industry standards and seller and buyer needs**. Competition is tough as the likes of PayPal are encroaching on its turf. Also, increasing competition from Shopify remains a headwind. These call for frequent changes in product and service offerings, which in turn require heavy investments, putting pressure on its earning capacity.
 - ▼ The nature of its business makes Square vulnerable to **foreign exchange risk**. Apart from the U.S., the company operates in Canada, Australia and Japan and derives a significant part of its sales and earnings from there. Thus, appreciation or depreciation of the U.S. dollar versus foreign currencies could impact the company's results.
 - ▼ Moreover, the company is trading at premium in terms of Price/Book (P/B). Square currently has a trailing 12-month P/B ratio of 20.88. This level compares unfavorably with what the industry witnessed in the last year. Additionally, the ratio is near the high end of the valuation range in this period. Consequently, the valuation looks slightly stretched from P/B perspective.
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Last Earnings Report

Square Surpasses Earnings & Revenues Estimates in Q4

Square reported fourth-quarter 2019 adjusted earnings of 23 cents per share, which beat the Zacks Consensus Estimate by 15%. The bottom line was also higher than management's guided range of 19-21 cents per share. Further, the figure improved 64.3% on a year-over-year basis but declined 8% sequentially.

Net revenues of \$1.31 billion surpassed the Zacks Consensus Estimate of \$1.19 billion and came ahead of the guided range of \$1.16-\$1.18 billion. The top line also improved 41% from the year-ago quarter and 3.7% sequentially.

We note that the company has stopped reporting adjusted revenues from fourth-quarter 2019 onwards.

The top line was driven by Seller ecosystem that contributed \$938 million to net revenues, up 26% year over year. Further, robust performance of Cash App, which generated \$361 million of net revenues, up 147% year over year, was a major positive. Furthermore, strengthening momentum across Bitcoin and rapid adoption of Cash Card contributed to the results.

Additionally, continued acceleration in gross payment volume (GPV) drove the results.

Notably, the company completed the divestiture of Caviar to DoorDash at the end of October 2019. Caviar had been underperforming and consequently its sale remains a major positive.

Excluding Caviar, net revenues would have exhibited growth of 46% on a year-over-year basis.

We believe the company's solid momentum across sellers and strong product portfolio is likely to continue aiding performance in the near term.

Gross Payment Volume

GPV in the fourth quarter amounted to \$28.64 billion beating the Zacks Consensus Estimate of \$28.54 billion. Notably, the figure improved 25% year over year and 1.5% on a sequential basis.

GPV growth was driven by the company's continued momentum across the larger sellers.

Square defines larger sellers as those that make more than \$125,000 of annualized GPV and mid-market sellers as those with annualized revenues of more than \$500,000.

GPV from larger sellers contributed 55% to total GPV, up 33% year over year. Further, Square witnessed strong contributions from mid-market sellers, which accounted for 27% of total GPV, up 42% from the year-ago quarter.

This can be attributed to Square's robust product portfolio and comprehensive ecosystem that aided the company in attracting new sellers to its platform while retaining the existing ones.

Additionally, robust Square Capital aided the company's momentum across the seller ecosystem. This was a positive. Further, expanding international presence of Square Terminal remained a tailwind.

Top-Line Details

Transaction (63.4% of net revenues): The company generated transaction revenues of \$832.2 million, up 25% year over year. Revenue growth within this category can be attributed to strengthening momentum across sellers.

Subscription and services (21.4% of revenues): The company generated \$281.4 million revenues from this category, surging 45% from the year-ago quarter. This improvement can be attributed to the strong performance by Cash App, which contributed \$183 million to the category's top line. Further, solid momentum across seller subscription and services products remained positive. Additionally, Square Capital, which facilitated 97,000 originations worth \$ 671 million, up 42% from the year-ago quarter, contributed to the results.

Hardware (1.7% of revenues): Square generated \$22.3 million of revenues from this business, up 23% year over year. The category's top line was primarily driven by robust Square Terminal and Square Reader for contactless and chip.

Bitcoin (13.5% of revenues): The company generated \$177.6 million revenues from this category, soaring 238.6% on a year-over-year basis. Square continued to benefit in the bitcoin space on the back of growing adoption of Cash App. Notably, without bitcoin revenues, Cash App revenues would have come in at \$183 million.

Operating Details

Per management, gross profit as a percentage of net revenues came in 40.1%, contracting 60 basis points (bps) year over year. While Transaction, Subscription and services and Bitcoin generated profit, Hardware category reported loss during the reported quarter.

Adjusted EBITDA as a percentage of net revenues was 9%, expanding 30 bps year over year.

Operating expenses came in \$509.7 million, surging 33% from prior-year quarter.

Product development expenses were \$173.3 million, up 22.2% year over year, primarily owing to growing engineering, data science and design

Quarter Ending	12/2019
Report Date	Feb 26, 2020
Sales Surprise	10.71%
EPS Surprise	15.00%
Quarterly EPS	0.23
Annual EPS (TTM)	0.19

personnel costs.

General and administrative expenses were \$118.2 million, up 23.8% from prior-year quarter. This was primarily owing to finance, legal and support personnel costs.

Further, sales and marketing costs were \$185.2 million, up 55.2% year over year, due to increase in Cash App peer-to-peer payment transfer and Cash Card issuances.

Balance Sheet

As of Dec 31, 2019, cash and cash equivalents balance was \$1.05 billion, up from \$612.04 million as of Sep 30, 2019.

Short-term investments were \$492.5 million in the reported quarter, down from \$557.6 million in the previous quarter.

Long-term debt was \$938.8 million, increasing from \$928.9 million in previous quarter.

Guidance

For first-quarter 2020, Square expects net revenues between \$1.34 billion and \$1.36 billion.

Gros profit is anticipated in the range of \$550-\$560 million.

Adjusted earnings are expected in the range of 16-18 cents per share.

For 2020, Square expects total net revenues between \$5.9 billion and \$5.96 billion.

Gros profit is anticipated to lie between \$2.44 billion and \$2.475 billion.

Adjusted earnings are projected in the range of 90-94 cents per share.

We note that mid-points of both earnings and revenue guided ranges for first-quarter 2020 and full year 2020 are above the Zacks Consensus Estimate.

Recent News

On **Nov 1, 2019**, Square completed the sale of Caviar to DoorDash.

On **Oct 24, 2019**, Square teamed up with simPRO. The partnership will enable both the companies to offer innovative mobile payment solution to the field service businesses. The move will aid Square to gain momentum across field service businesses.

Valuation

Square shares are up 36.4% in the past six-month period and 11.6% over the trailing 12-month period. While stocks in the Zacks sub-industry are down 0.8%, the same in the Zacks Computer & Technology sector are up 9.6% in the past six-month period. Over the past year, the Zacks sub-industry and the sector are up 3.8% and 12.5%, respectively.

The S&P 500 index is up 2.1% in the past six-month period and 4.9% in the past year.

The stock is currently trading at 5.87X forward 12-month sales, which compares to 6.11X for the Zacks sub-industry, 3.34X for the Zacks sector and 3.12X for the S&P 500 index.

Over the past three years, the stock has traded as high as 10.2X and as low as 2.67X, with a 3-year median of 5.8X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$87 price target reflects 6.13X forward 12-month sales.

The table below shows summary valuation data for SQ

Valuation Multiples - SQ					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	5.87	6.11	3.34	3.12
	3-Year High	10.2	6.66	3.58	3.43
	3-Year Low	2.67	4.73	2.62	2.76
	3-Year Median	5.8	5.73	3.19	3.15
P/B TTM	Current	20.88	7.09	4.53	3.96
	3-Year High	37.25	8.23	5.34	4.54
	3-Year Low	9.76	3.14	3.57	3.36
	3-Year Median	22.69	6.04	4.53	3.92
EV/Sales TTM	Current	7.49	6.86	3.88	2.96
	3-Year High	14.79	7.64	4.19	3.42
	3-Year Low	3.11	3.41	3.05	2.45
	3-Year Median	7.41	6.13	3.75	2.97

As of 02/28/2020

Industry Analysis Zacks Industry Rank: Top 42% (106 out of 254)



Top Peers

Automatic Data Processing, Inc. (ADP)	Neutral
Alphabet Inc. (GOOGL)	Neutral
Intuit Inc. (INTU)	Neutral
PayPal Holdings, Inc. (PYPL)	Neutral
Wix.com Ltd. (WIX)	Neutral
The Western Union Company (WU)	Neutral
MoneyGram International Inc. (MGI)	Underperform
Shopify Inc. (SHOP)	Underperform

Industry Comparison Industry: Internet - Software				Industry Peers		
	SQ Neutral	X Industry	S&P 500	INTU Neutral	PYPL Neutral	SHOP Underperform
VGM Score	D	-	-	B	C	D
Market Cap	35.81 B	624.68 M	21.48 B	69.25 B	126.67 B	53.44 B
# of Analysts	13	5	13	10	16	24
Dividend Yield	0.00%	0.00%	2.07%	0.80%	0.00%	0.00%
Value Score	F	-	-	D	D	F
Cash/Price	0.03	0.11	0.04	0.03	0.08	0.04
EV/EBITDA	832.77	-1.76	12.57	31.76	30.91	-847.42
PEG Ratio	2.28	2.39	1.84	2.24	1.70	89.85
Price/Book (P/B)	20.88	5.37	2.88	18.58	7.48	17.72
Price/Cash Flow (P/CF)	222.53	33.17	11.58	40.71	33.17	NA
P/E (F1)	90.58	48.68	16.87	35.14	31.30	2,246.35
Price/Sales (P/S)	7.60	3.95	2.34	9.72	7.13	33.86
Earnings Yield	1.10%	0.74%	5.91%	2.85%	3.19%	0.05%
Debt/Equity	0.61	0.12	0.70	0.10	0.29	0.00
Cash Flow (\$/share)	0.37	-0.01	6.94	6.53	3.26	-0.60
Growth Score	B	-	-	A	A	A
Hist. EPS Growth (3-5 yrs)	NA%	16.66%	10.85%	24.52%	20.43%	NA
Proj. EPS Growth (F1/F0)	14.52%	12.10%	6.79%	12.07%	11.31%	-31.25%
Curr. Cash Flow Growth	130.71%	2.63%	5.92%	18.22%	30.28%	85.89%
Hist. Cash Flow Growth (3-5 yrs)	22.37%	15.53%	8.38%	9.68%	18.18%	NA
Current Ratio	1.90	1.56	1.23	1.67	1.43	8.68
Debt/Capital	37.92%	18.57%	42.53%	9.10%	22.68%	0.00%
Net Margin	7.97%	-16.29%	11.57%	22.89%	13.84%	-7.91%
Return on Equity	6.57%	-14.59%	16.80%	41.03%	17.33%	-2.69%
Sales/Assets	1.07	0.63	0.54	1.09	0.36	0.55
Proj. Sales Growth (F1/F0)	19.06%	18.43%	4.07%	10.86%	17.56%	37.35%
Momentum Score	F	-	-	B	C	F
Daily Price Chg	5.07%	0.00%	-1.44%	-1.09%	0.14%	5.69%
1 Week Price Chg	1.99%	-1.00%	-0.94%	-2.21%	-2.85%	-1.99%
4 Week Price Chg	9.50%	-7.08%	-10.98%	-7.25%	-7.80%	-2.85%
12 Week Price Chg	24.11%	0.00%	-7.84%	4.76%	3.25%	27.43%
52 Week Price Chg	2.57%	-13.02%	1.20%	7.57%	10.12%	144.94%
20 Day Average Volume	8,981,726	262,006	2,169,477	1,246,452	7,068,067	2,672,766
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.19%	0.00%	-4.39%
(F1) EPS Est 4 week change	-24.29%	0.00%	-0.09%	0.19%	0.09%	-113.59%
(F1) EPS Est 12 week change	-37.03%	-3.45%	-0.24%	0.10%	-0.10%	-116.01%
(Q1) EPS Est Mthly Chg	-30.00%	-0.81%	-0.72%	-4.23%	-6.31%	-132.27%

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	B
Momentum Score	F
VGM Score	D

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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