

Square, Inc. (SQ)

\$85.24 (As of 02/19/20)

Price Target (6-12 Months): **\$90.00**

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:C

Value: F

Growth: A

Momentum: F

Summary

Square continues to benefit from growing gross payments volume. The company's seller ecosystem, which helps in strengthening relationship with sellers, is contributing significantly to the payment volume growth. Further, robust Square Terminal, Instant Deposits, Cash Card, Square Register and Square Capital continue to drive the top line. Further, growing adoption of Cash App in the bitcoin space remains a major positive. We believe the company's solid momentum across sellers and strong product portfolio is likely to continue aiding performance in the near term. However, higher investments and increasing product development expenses might hurt margins. Further, intensifying competition and foreign exchange fluctuations remain woes. Notably, the stock has underperformed the industry it belongs to in the past year.

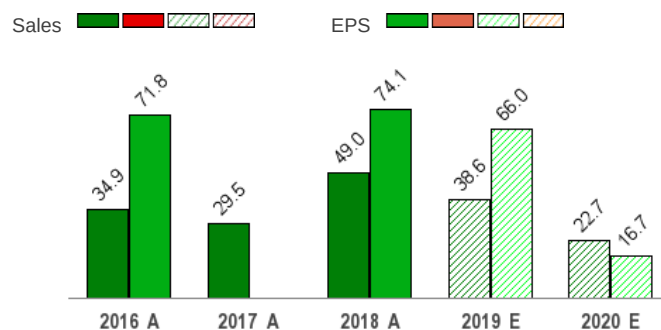
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$86.48 - \$54.41
20 Day Average Volume (sh)	7,749,136
Market Cap	\$36.6 B
YTD Price Change	36.3%
Beta	3.26
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Internet - Software
Zacks Industry Rank	Top 40% (103 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	25.0%
Last Sales Surprise	9.8%
EPS F1 Est- 4 week change	-25.4%
Expected Report Date	02/26/2020
Earnings ESP	3.6%
P/E TTM	120.1
P/E F1	93.7
PEG F1	2.4
P/S TTM	8.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	1,196 E	1,407 E	1,504 E	1,504 E	5,612 E
2019	959 A	1,174 A	1,266 A	1,186 E	4,572 E
2018	669 A	815 A	882 A	933 A	3,298 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$0.14 E	\$0.21 E	\$0.27 E	\$0.29 E	\$0.91 E
2019	\$0.11 A	\$0.21 A	\$0.25 A	\$0.20 E	\$0.78 E
2018	\$0.06 A	\$0.13 A	\$0.13 A	\$0.14 A	\$0.47 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 02/19/2020. The reports text is as of 02/20/2020.

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 \$3.3 billion in 2018. The company earns revenues from transactions, subscription and services, hardware and bitcoin.

Transaction-based revenues (75% of total revenues in 2018) include transaction fees that sellers pay for managed payment solutions and services.

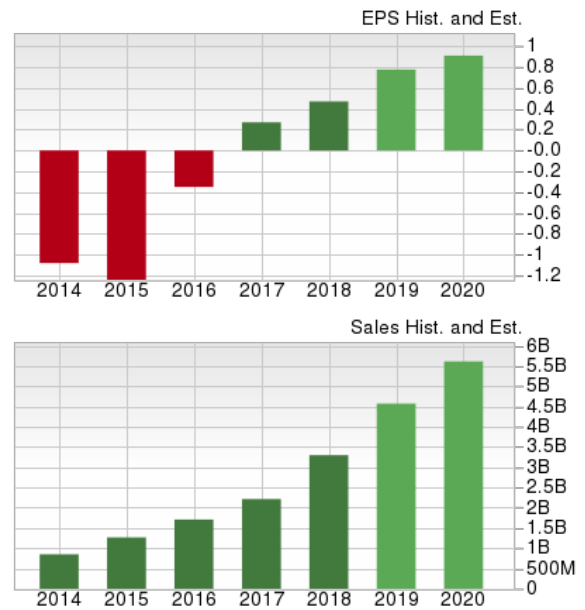
Subscription and services-based revenues (17.9%) include fees that sellers pay for a range of paid services-based products including Square Appointments, Gift Cards, Customer Engagement, Employee Management, Payroll, Instant Deposit, and other subscription and services-based products offered through 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 (2.1%) 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 (5%) are derived from total sales of bitcoin to customers. Cash App users can buy and sell bitcoins.

Geographically, the United States contributed almost 95.2% of revenues, while the rest came from International markets.

The company had approximately 3,349 employees worldwide as of Dec 31, 2018.



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 \$84.7 billion of Gross Payment Volume (GPV) in 2018. The company has been doing well with larger and midmarket sellers. In third-quarter 2019, larger sellers contributed 55% to total GPV, up 34% 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:

- ▼ **Square has been incurring losses** over the last few years. The company reported net loss of \$38.5 million, \$62.8 million and \$171.6 million in 2018, 2017 and 2016, respectively. Moreover, Square profits remain at risk due to higher-than-expected fraud and bad debt cost in the near future. Further, the company continues to invest significantly in sales and marketing, product and service development, infrastructure development and expansion of international operations. So there is no clear path to profitability in the foreseeable future.
- ▼ 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.

Square is currently a loss making business and vulnerable to intense competition and changing technology, industry standards and seller and buyer needs.

Last Earnings Report

Square Surpasses Earnings & Revenues Estimates in Q3

Square reported third-quarter 2019 adjusted earnings of 25 cents per share, which beat the Zacks Consensus Estimate by 25% and was higher than management's guided range of 18-20 cents per share. Further, the figure improved 92.3% on a year-over-year basis and 19% sequentially.

Net revenues of \$1.27 billion surpassed the Zacks Consensus Estimate of \$1.15 billion and came ahead of the guided range of \$1.13 billion to \$1.15 billion. The figure improved 44% from the year-ago quarter and 8.5% sequentially.

Per management, adjusted revenues came in \$602.2 million, up 40% year over year and 7% from the prior quarter. The figure was also higher than management's guided range of \$590-\$600 million.

The top line was driven by Seller ecosystem that contributed \$918 million to net revenues, up 27% year over year. Further, robust performance of Cash App during the reported quarter was a major positive. Furthermore, strengthening adoption rate of Bitcoin and Cash Card contributed to the results.

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

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

Gross Payment Volume

GPV in the third quarter amounted to \$28.23 billion beating the Zacks Consensus Estimate of \$27.95 billion. Notably, the figure improved 25.5% year over year and 5.4% on a sequential basis.

Year-over-year 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 34% year over year. Further, Square witnessed strong contributions from mid-market sellers who accounted for 27% of total GPV, up 44% from the year-ago quarter.

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

Additionally, robust Square Terminal and Square Register continued to contribute to GPV growth.

Top-Line Details

Transaction (64.5% of net revenues): The company generated transaction revenues of \$816.6 million, up 24.6% year over year. Revenue growth within this category can be attributed to strengthening momentum across sellers and well-performing Cash App.

Subscription and services (22.1% of revenues): The company generated \$279.8 million revenues from this category, soaring 68.3% from the year-ago quarter. This improvement can be attributed to the strong performance by Cash App and Instant Deposit. Further, Square Capital, which facilitated \$563 million of business loans during the third quarter, up 39% year over year, contributed to the category's revenues.

Hardware (1.7% of revenues): Square generated \$21.8 million of revenues from this business, up 23.9% year over year. The top line within this category was primarily driven by robust Square Terminal.

Bitcoin (11.7% of revenues): The company generated \$148.3 million revenues from this category, soaring 245.1% on a year-over-year basis. Square continues to benefit in the bitcoin space on the back of growing momentum of Cash App among users.

Operating Details

Per management, gross profit as a percentage of net revenues came in 39.5%, contracting 40 bps year over year. Although Transaction, Subscription and services and Bitcoin generated profit, Hardware category generated loss during the reported quarter.

Adjusted EBITDA as a percentage of adjusted revenues was 21.8%, expanding 530 bps year over year.

Operating expenses came in \$467.9 million, surging 29% from prior-year quarter.

Product development expenses were \$168.8 million, up 24.3% year over year, primarily owing to growing engineering, data science and design personnel costs.

General and administrative expenses were \$115.9 million, up 35.6% from prior-year quarter. This was primarily owing to finance, legal and support personnel costs.

Further, sales and marketing costs were \$149.5 million, up 28.5% year over year, due to increase in Cash App peer-to-peer payment transfer and Cash Card issuances.

Quarter Ending **09/2019**

Report Date	Nov 06, 2019
Sales Surprise	9.77%
EPS Surprise	25.00%
Quarterly EPS	0.25
Annual EPS (TTM)	0.71

Balance Sheet

As of Sep 30, 2019, cash and cash equivalents balance was \$612.04 million, down from \$617.28 million as of Jun 30, 2019.

Short-term investments were \$557.6 million in the reported quarter, down from \$572.2 million in the previous quarter.

Long-term debt was \$928.9 million, increasing from \$919 million in previous quarter.

Guidance

For fourth-quarter 2019, Square expects net revenues between \$1.16 billion and \$1.18 billion.

Further, adjusted revenues are anticipated in the range of \$585-\$595 million. Adjusted EBITDA is expected in the band of \$112-\$117 million.

Adjusted earnings are expected in the range of 19-21 cents per share.

For 2019, Square raised the guided range for total net revenues from \$4.41-\$4.47 billion to \$4.56-\$4.58 billion.

Further, management revised adjusted revenue guidance downward from \$2.25-\$2.28 billion to \$2.24-\$2.25 billion. Adjusted EBITDA is anticipated in the range of \$410-\$415 million.

Adjusted earnings are projected in the range of 76-78 cents per share.

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 30.3% in the six-month period and 14.6% over the trailing 12-month period. Stocks in the Zacks sub-industry are up 4.9% and 21.6% for Zacks Computer & Technology sector in the six-month period, respectively. Over the past year, the Zacks sub-industry and the sector is up 14.9% and 29.5%, respectively.

The S&P 500 index is up 15.8% in the six-month period and 20.7% in the past year.

The stock is currently trading at 6.35X forward 12-month sales, which compares to 6.79X for the Zacks sub-industry, 3.78X for the Zacks sector and 3.57X for the S&P 500 index.

Over the past three years, the stock has traded as high as 10.2X and as low as 1.65X, with a 3-year median of 4.92X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$90 price target reflects 6.7X 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	6.35	6.79	3.78	3.57
	3-Year High	10.2	15.61	3.78	3.57
	3-Year Low	1.65	3.06	2.3	2.54
	3-Year Median	4.92	5.35	3.02	3
P/B TTM	Current	23.24	6.83	5.37	4.42
	3-Year High	37.25	8.17	5.38	4.45
	3-Year Low	5.52	2.28	3.13	2.85
	3-Year Median	20.49	5.16	4.21	3.6
EV/Sales TTM	Current	6.67	6.62	4.42	3.02
	3-Year High	14.79	11.57	4.42	3.29
	3-Year Low	1.73	3.01	2.56	2.43
	3-Year Median	6.3	6.01	3.44	2.9

As of 02/19/2020

Industry Analysis Zacks Industry Rank: Top 40% (103 out of 255)



Top Peers

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

Industry Comparison Industry: Internet - Software				Industry Peers		
	SQ Neutral	X Industry	S&P 500	INTU Neutral	PYPL Neutral	SHOP Neutral
VGM Score	C	-	-	F	C	C
Market Cap	36.63 B	739.33 M	24.59 B	79.55 B	145.34 B	62.66 B
# of Analysts	13	5	13	10	16	25
Dividend Yield	0.00%	0.00%	1.78%	0.69%	0.00%	0.00%
Value Score	F	-	-	F	D	F
Cash/Price	0.03	0.11	0.04	0.03	0.07	0.04
EV/EBITDA	851.65	-2.32	14.21	36.76	35.69	-1,000.60
PEG Ratio	2.36	2.71	2.09	2.57	1.95	24.85
Price/Book (P/B)	29.26	5.64	3.28	21.90	8.59	20.78
Price/Cash Flow (P/CF)	509.74	38.06	13.59	46.80	38.06	NA
P/E (F1)	93.67	53.82	19.17	40.35	35.90	621.24
Price/Sales (P/S)	8.45	4.70	2.68	11.47	8.18	39.70
Earnings Yield	1.07%	0.69%	5.18%	2.48%	2.78%	0.16%
Debt/Equity	0.83	0.11	0.70	0.18	0.29	0.00
Cash Flow (\$/share)	0.17	-0.01	6.93	6.53	3.26	-0.60
Growth Score	A	-	-	F	A	A
Hist. EPS Growth (3-5 yrs)	NA%	16.66%	10.84%	24.52%	20.43%	NA
Proj. EPS Growth (F1/F0)	17.20%	13.19%	7.00%	12.22%	11.35%	191.47%
Curr. Cash Flow Growth	-2,039.38%	2.02%	7.81%	18.22%	30.28%	85.89%
Hist. Cash Flow Growth (3-5 yrs)	22.37%	14.75%	8.25%	9.68%	18.18%	NA
Current Ratio	1.68	1.58	1.24	1.80	1.43	8.68
Debt/Capital	45.31%	15.66%	42.37%	15.57%	22.68%	0.00%
Net Margin	-1.01%	-14.43%	11.69%	22.79%	13.84%	-7.91%
Return on Equity	5.72%	-13.19%	16.86%	42.04%	17.33%	-2.69%
Sales/Assets	1.06	0.64	0.55	1.12	0.36	0.55
Proj. Sales Growth (F1/F0)	22.75%	18.39%	4.05%	10.74%	17.56%	35.34%
Momentum Score	F	-	-	C	D	B
Daily Price Chg	3.42%	0.00%	0.38%	0.67%	1.34%	1.27%
1 Week Price Chg	3.80%	1.97%	1.65%	3.25%	3.46%	10.97%
4 Week Price Chg	24.09%	0.12%	0.86%	5.19%	7.28%	16.88%
12 Week Price Chg	22.38%	9.24%	4.56%	16.58%	15.00%	59.30%
52 Week Price Chg	12.20%	-2.00%	14.15%	29.51%	30.80%	203.11%
20 Day Average Volume	7,749,136	244,961	1,989,235	942,309	6,535,496	2,390,057
(F1) EPS Est 1 week change	-22.06%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-25.35%	0.00%	-0.03%	0.00%	0.09%	0.73%
(F1) EPS Est 12 week change	-37.03%	0.00%	-0.21%	-0.21%	-0.10%	0.39%
(Q1) EPS Est Mthly Chg	-44.44%	0.00%	-0.40%	0.00%	-6.31%	0.88%

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	F
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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